IRS CRIMINAL INVESTIGATION

THE USE OF BIG DATA AND DETERRENCE TO ACHIEVE VOLUNTARY COMPLIANCE

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IRS Use of Big Data in Tax Enforcement

How did We Get Here?

• IRS must do more with fewer resources
• IRS budget reduced by $900M
• IRS staff decreased by >17,000 people
• Average annual tax gap of $458B
Data Analytics to Enhance Compliance

• Identity Theft Prevention – Filters contributed to the protection of $6 billion in revenue in 2017

• Redesigning Notices – Improved taxpayer compliance through redesigned notices; up 11 percent in payment compliance resulting in $650 million in additional collection and 31% increase in use of self-service tools and 20% decrease in IRS costs

• Compliance Risk Assessment – Use of predictive models with subject matter experts to assess risk for large corporations and pass-through entities have already identified previously unrecognized areas of noncompliance among partnerships

• Employment Tax Investigations – Algorithms have identified 18 cases with an average tax loss of 30% greater than traditional methods, e.g., $3 million versus $2.3 million

• Exam Selection – Evaluated 250 data elements in multi-phase statistical algorithm focused on changes on Employee Plan returns that exceeded past results by more than 20%.
INTERNAL REVENUE SERVICE
CRIMINAL INVESTIGATION
CI as a Federal Law Enforcement Agency

**Mission**
To serve the American public by investigating potential criminal violations of the Internal Revenue Code and related financial crimes in a manner that fosters confidence in the tax system and compliance with the law.

**Organization / History**
Formed in 1919, CI is the 6th largest Federal Law Enforcement Agency (Treasury’s largest) comprised of 2,767 employees worldwide, 2,030 of whom are special agents and 737 professional staff employees. CI’s investigative jurisdiction includes tax, money laundering and Bank Secrecy Act (BSA) laws. Some of the most notorious tax cheats in CI’s history include mobsters Al Capone and John Gotti, politicians Vice President Spiro Agnew and Representative James Traficant, international corporations including soccer’s FIFA and banking giant UBS, real estate magnet Leona Helmsley, baseball great Pete Rose, and performers Chuck Berry and Willie Nelson.

**Program Areas**
Employment Tax / International Tax Fraud / Abusive Tax Schemes / General Tax Fraud / Cyber Crimes / Cryptocurrency & Virtual Currency / Refund Fraud (Stolen Identity Refund, Questionable Refund, and Return Preparer) / Organized Crime Drug Enforcement Task Force (OCDETF) / Terrorism / Public Corruption

**Direct Investigative Time**
CI spends over 75% of Direct Investigative Time investigating tax violations. 11% high level OCDETF/Narcotics, 14% other significant financial crimes (high level money laundering, terrorist financing, cyber crimes, BSA violations.)

**Investigative Jurisdiction**
While other federal agencies also have investigative jurisdiction for money laundering and some BSA violations, **CI is the only federal agency authorized to investigate potential criminal violations of the Internal Revenue Code** and the only federal agency solely devoted to investigating financial crimes. CI’s expertise in following the money is highly sought by DOJ in the most significant financial investigations.
The Challenge of Criminal Tax Enforcement

Criminal Tax Prosecutions

- **326M** U.S. residents filing **245M** tax returns/forms

- **1,224**: CI’s 20 year annual average for tax prosecution authorizations

- Criminal tax cases drive the deterrent message to all taxpayers and U.S. citizens

- CI is a critical component to voluntary compliance

- Numerous Critical Program Areas
# Our Priorities – At a Glance

<table>
<thead>
<tr>
<th>Investigative Priority</th>
<th>Case Examples</th>
<th>Highlights</th>
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</thead>
<tbody>
<tr>
<td><strong>GENERAL FRAUD</strong></td>
<td>Bill Melot – New Mexico Farmer</td>
<td>Sentenced to 14 years in prison for tax evasion and program fraud; Ordered to pay restitution to IRS of $18.4 million</td>
</tr>
<tr>
<td><strong>RETURN PREPARER FRAUD</strong></td>
<td>Gladstone &amp; Jacqueline Morrison</td>
<td>Sentenced to 187 months each; Order to pay nearly $18 million on restitution</td>
</tr>
<tr>
<td><strong>ABUSIVE TAX SCHEMES</strong></td>
<td>Credit Suisse</td>
<td>Guilty plea - conspiracy to aid U.S. taxpayers in filing false returns; agreed to pay $2.6 billion</td>
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<td></td>
<td>Bank Julius Baer</td>
<td>Deferred Prosecution Agreement and admitted to helping US taxpayers file false tax returns; $547 million restitution</td>
</tr>
<tr>
<td><strong>EMPLOYMENT TAX FRAUD</strong></td>
<td>Tammy Devier</td>
<td>Sentenced to 60 months and convicted of Failure to Pay Over Employment Taxes</td>
</tr>
<tr>
<td><strong>CYBER CRIMES AND VIRTUAL CURRENCY</strong></td>
<td>Liberty Reserve and Silk Road</td>
<td>LR: was one of the world's largest virtual currency companies, indicted for allegedly running $6B money laundering scheme. SR: used by more than 100,000 users to buy and sell illegal drugs and other unlawful goods and services</td>
</tr>
<tr>
<td><strong>TERRORIST FINANCING</strong></td>
<td>Jimenez and Robertson</td>
<td>Guilty of filing false returns to fund travel to Syria</td>
</tr>
<tr>
<td><strong>PUBLIC CORRUPTION</strong></td>
<td>Kwame Kilpatrick</td>
<td>Sentenced to 336 months</td>
</tr>
<tr>
<td><strong>TRANSNATIONAL ORGANIZED CRIME</strong></td>
<td>FIFA</td>
<td>Uncovered widespread corruption in international soccer. Forty-two subjects charged to date. Restitution exceeds $190 million</td>
</tr>
<tr>
<td><strong>FRIVOLOUS ARGUMENTS</strong></td>
<td>Ronald Joling</td>
<td>Sentenced to 97 months for obstructing the IRS; Restitution of $1.2 million</td>
</tr>
<tr>
<td><strong>ORGANIZED CRIME DRUG ENFORCEMENT TASK FORCES</strong></td>
<td>Edgar Manual Valencia Ortega – Sinaloa Cartel money launderer</td>
<td>Sentenced to 96 months for laundering money on behalf of Chapo Guzman</td>
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<tr>
<td><strong>IDENTITY THEFT</strong></td>
<td>Rashia Wilson, Self-Proclaimed Queen of Tax Fraud</td>
<td>Serving 21 year prison term</td>
</tr>
</tbody>
</table>
Data & Data Analytics…One Answer to the Challenge

**CI’s Data Vision**

CI has dedicated significant resources to pivot to a data-driven law enforcement agency by utilizing data and data analytics to drive case selection and development decisions, as well as, address emerging threats to its overall mission of criminal tax enforcement and related financial crimes.

**Traditional Approach to Case Development**

- Special agent dependent
- IRS Civil dependent
- Federal/State/Local agency dependent
- Archaic, manual research methods

**New Data Driven Approach to Case Development**

- Using data scientists to analyze voluminous internal and external data
- Quickly analyzing large pools of data using tools such as Palantir, which integrates and conducts searches on more than 40 internal/external data sets in a matter of seconds
- Leveraging existing data and acquiring new data sets (from regulatory and law enforcement agencies)
- IRS cross business operating division collaboration (one enterprise approach)
- Industry and academia collaboration (data analytic firms and universities)
- Nationally Coordinated Investigations Unit

**CI’s Use of Big Data**

- CI is in the early stages of using data analytics and modeling to identify areas of non-compliance
- CI has added a new “Data Section”
- Encourage all CI personnel to adopt a data mindset

*These initiatives represent FY 2019 NCIU priorities.*
CI’s Use of Big NCIU Results: FY 2018 – 55 cases referred to all 25 field offices; FY 2019 – 106 cases referred to all 21 field offices:

<table>
<thead>
<tr>
<th>Initiative</th>
<th># of Referrals</th>
<th>Estimated Aggregate Tax Loss/ML Amount</th>
<th>Estimated Average Tax Loss/ML Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Biofuels Credit</td>
<td>3</td>
<td>$25,819,853</td>
<td>$8,606,618</td>
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<tr>
<td>Employment Tax*</td>
<td>119</td>
<td>$294,591,589</td>
<td>$2,475,560</td>
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<tr>
<td>International - FATCA*</td>
<td>6</td>
<td>$25,479,583</td>
<td>$4,246,597</td>
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<tr>
<td>International - USCLA*</td>
<td>1</td>
<td>$1,273,321</td>
<td>$1,273,321</td>
</tr>
<tr>
<td>International - Other*</td>
<td>7</td>
<td>$148,628,636</td>
<td>$21,232,662</td>
</tr>
<tr>
<td>Microcap Stock</td>
<td>12</td>
<td>$17,015,747</td>
<td>$1,417,979</td>
</tr>
<tr>
<td>National Targeting Center*</td>
<td>5</td>
<td>$17,500,000</td>
<td>$3,500,000</td>
</tr>
<tr>
<td>Narcotics, Counter-Terrorism, and TCO</td>
<td>1</td>
<td>$100,000</td>
<td>$100,000</td>
</tr>
<tr>
<td>TEGE</td>
<td>1</td>
<td>$1,080,182</td>
<td>$1,080,182</td>
</tr>
<tr>
<td>Virtual Currency*</td>
<td>5</td>
<td>$12,582,651</td>
<td>$2,516,530</td>
</tr>
<tr>
<td>Whistleblower*</td>
<td>1</td>
<td>$209,750</td>
<td>$209,750</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>161</strong></td>
<td><strong>$544,281,312</strong></td>
<td><strong>$3,380,629.27</strong></td>
</tr>
</tbody>
</table>

* These initiatives represent FY 2019 NCIU priorities.
One Example…The Employment Tax Initiative

- A Data Driven Approach
- A New, Combined Data Set
  - NCIU Employment Tax Model
  - Focus on internal datasets with a new approach
  - Combine and add in law enforcement/FinCEN Data
- Collaboration with RAAS
  - Compliance Data Warehouse
- New Cases Developed Versus Traditional Methods
  - Close to 80 referrals with an average tax loss of approximately $2.9M
  - All 21 CI Field Offices Impacted
  - Pivot back to Core Mission Tax Investigations
New Non-Compliant Population Found

Non-Compliance Criteria

- Did **NOT** file a Form 941/944 and did **NOT** make a payment
- Did **NOT** file a Form 941/944 but did make a payment
- Did file a Form 941/944 but **did NOT** make a payment

Employers
- No W-2s with SSA
- Employees submitted W-2s with IRS

Employers
- Submitted W-2s with SSA
- Employees submitted W-2s with IRS
- Overlaps with CAWR report
Nationwide Coverage & Deterrent Impact

Heat map of potential employment tax cases (692,000 dots)
CI selected Palantir as their primary data analytics tool in 2014. Palantir can capture, curate, store, search, share, transfer, analyze and visualize the metadata associated with a case or lead, perform link analysis, entity resolution and de-confliction, and includes advanced analytical abilities to conduct relational, temporal, geospatial, statistical and behavioral analysis, and collaboration to turn raw data into actionable intelligence.

CI uses Palantir for Lead Generation & Case Development

- 2900+ Users
- 61 Data Collections Tax/BSA & User Imported Data
- 9.5+ Billion Records including Tax, Bank Secrecy Act FinCEN, Panama Papers, Dark Web Identifiers, Swiss Bank Project, Industry Leads
- 1M Search Requests Per Month
- $100s of Millions in Fraud Identified
In Conclusion…

- Data Analytics Allows IRS-CI to Shine a Light in the Dark Corners of Tax Non-Compliance

- Data Analytics Better Enables the IRS to Protect the Tax System by Identifying and Investigating the Most Egregious Offenders

- Data Analytics is the Future of Tax Compliance and Empowers the IRS to More Efficiently Utilize Our Limited Resources and Be Good Stewards of Taxpayer Dollars

- The Efficient Use of Data by the IRS is a Win For Everyone… Except the Criminals Who Are Intentionally Failing to Meet Their Tax Obligations

- Data Analytics will Help Protect America’s Tax and Financial System, While Helping Ensure A Fair and Level Playing Field for All Taxpayers
Welcome IRS Area Counsel Criminal Tax!

Division Counsel/Associate Chief Counsel (Criminal Tax) plans, directs, and coordinates policies and programs with respect to substantive criminal matters, criminal procedure, and investigative matters, including:

- Tax, currency, and money laundering crimes
- Administrative and grand jury investigations
- Undercover operations and non-consensual electronic surveillance
- Search warrants and forfeitures
- Proposed Grants of Immunity under 18 U.S.C. § 6001, et seq.; Referral of cases to the Department of Justice (DOJ) for prosecution or commencement of judicial forfeitures; Providing appellate recommendations to DOJ

Area Counsel (Criminal Tax) is responsible for advising and counseling the Director, Field Operations and the Special Agents in Charge, in all legal aspects of the criminal tax function. IRM 1.1.6.14
Big Data ~ Hot Topics
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IRS Summons and the Attorney-Client Privilege

irstaxtrouble.com
Big Data ~ Hot Topics
Big Data ~ Hot Topics
Universe of Big Data

Public and Commercial Data
- Social media (i.e., Twitter, Facebook, Instagram)
- Credit reports
- City and state records (i.e., deeds and registries)
- Credit/debit card processors
- eBay/PayPal
- Marketing data

IRS Data
- IRS Proprietary databases
- Prior tax returns and information returns
- Data collected from third parties
  - Examples: Dark web; Coinbase summons; offshore John Doe summonses
Client intake questions should include a full understanding of the client’s digital footprint; e.g., social media, online sales, cryptocurrency activity.

Advise clients to be mindful about what they post on social media.

Be aware of client’s suppliers and customer digital postings.

Follow developments in technology to stay abreast of changes in the IRS new technology.

Recent court cases and FOIA requests reflect that the IRS has acquired the ability to monitor phone traffic (Stingray phone tracking technology); emails (Electronic Communications Privacy Act court orders); and publicly available social media (Facebook).
BIG DATA & THE LAW

- Privacy Act of 1974
- Data Quality Act of 2001 ("Information Quality Act")
- 26 USC Section 7602
- 26 USC Section 6103
- 5 USC Section 552a
- Electronic Communications Privacy Act of 1986
- United States Constitution
“You’ll be happy to hear that Big Data confirms we can’t wring another penny out of you.”
THANK YOU!!