Structuring Transactions and Currency Violations: The "Tax Crime" of the Future!

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Charles Rettig and Edward Robbins highlight the various methods of money laundering and the IRS's efforts to combat such schemes.

"Money laundering" generally refers to financial-related transactions that are undertaken for the purpose of hiding or concealing the true source and/or ownership of the funds involved. It also includes various methods by which illegal-source funds are made to appear legitimate inherently facilitating the evasion of a variety of taxes. Since the events of September 11, 2001, money laundering has expanded to include the movement of funds for the purpose of supporting terrorist activities. Currently, it is believed that at least $3 trillion may be laundered annually worldwide. The ability to launder money enables those disguising the source of funds to promote, conceal and finance their activities and to enjoy their profits without obviously unwanted government interference.

Tax and money laundering violations are closely related and often involve similar activities. Since laundered funds are rarely reported on tax returns, money laundering is an integral part of many tax evasion schemes. The IRS Small Business/Self-Employed (SB/SE) Division maintains an anti-money laundering (AML) territory manager in each of its 16 areas, together with 33 AML compliance groups and 350 full-time examiners. IRS Criminal Investigation's Suspicious Activity Report (SAR) review teams in each of their 35 field offices focus on detecting money laundering activities as well as legal and illegal source tax schemes. There are at least 100 special agents around the country fully devoted to the detection and prevention of money-laundering activities. To effectively utilize its resources, the IRS frequently targets high-profile money laundering investigations, particularly those that will directly or indirectly enhance tax compliance.

Money laundering generally involves the placement of funds where cash is converted to monetary instruments deposited in

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multiple accounts in various financial institutions. These funds are typically layered through a series of financial transactions in an attempt to obscure their origin. Thereafter, the funds are often used to acquire legitimate assets and businesses funding future activities. These separate stages of the money laundering process are connected by the "paper trail" generated by the financial transactions. Money launderers intentionally avoid the reporting and recordkeeping requirements in an effort to avoid creating the paper trail.

Complex money laundering schemes often involve numerous financial transactions, intricate details and financial outlets located throughout the world. [IRS-CI] has the financial investigators and expertise that is critical to "follow the money trail."

IRS Involvement in Money Laundering Investigations

Most criminal activity involves crimes motivated by money, including tax evasion, embezzlement, public corruption, health care fraud, money laundering and various forms of narcotics trafficking. As such, the IRS is typically an important investigative agency in all money laundering investigations even if otherwise coordinated by other federal, state and local law enforcement authorities.

Complex money laundering schemes often involve numerous financial transactions, intricate details and financial outlets located throughout the world. IRS Criminal Investigation (IRS-CI) has the financial investigators and expertise that is critical to "follow the money trail." IRS-CI is a primary component of the National Money Laundering Strategy designed in coordination with the federal government's various anti–money laundering efforts. To further the goals of the National Money Laundering Strategy, the Department of Treasury allocates approximately $3 million per year to IRS-CI to staff task forces located in High Intensity Financial Crime Areas (HIFCA). HIFCAs may be geographically defined or may be created to address money laundering in an industry sector, a financial institution or a group of institutions. Enforcement funds are also used to support other money laundering task forces, SAR review teams, and for the ongoing development and maintenance of an electronic Bank Secrecy Act (BSA)[1] report filing system for the Financial Crimes Enforcement Network (FinCEN). There are ongoing efforts to allow the IRS to further increase its enforcement spending budget by $500 million over prior years. Appropriately funding the IRS enforcement efforts has historically been demonstrated to be a sound and wise investment.

When someone has a large amount of unreported income, he often attempts to conceal or launder it to make it appear as if it was from a legitimate or nontaxable source, allowing him to spend it or invest it in assets without much concern for the IRS and the attendant tax consequences. Some attempt to launder unreported proceeds by moving the money out of the United States and then bringing it back in a disguised form, often designated as loan proceeds or the recovery of a capital investment. Another method is to commingle the money within various business activities giving the appearance that the money was derived from a legal source or offset by legitimate business expenditures.

Financial investigations are extremely document-intensive and involve a thorough review of detailed records, such as bank or brokerage account information or real estate files, demonstrating the sequence of events involving the movement of money. Financial investigators attempt to identify and document money movements during the execution of a financial crime. The link between the source of the money, who receives it, when it is received and where it is deposited, may provide proof of criminal activity. A complete detailed financial analysis and reconstruction of the illegal activity (whether an embezzlement, skimming operation or an abusive trust scheme) documents the financial activities related to tax evasion and money laundering, often leading to a conviction.

History of IRS-CI and Money Laundering

On July 1, 1919, the IRS Commissioner created the Intelligence Unit to investigate widespread allegations of tax fraud by transferring six U.S. Post Office Inspectors to the Bureau of Internal Revenue to become the first Special Agents in charge of the organization that would one day become IRS-CI.

They built the Intelligence Unit into an elite group of highly trained, dedicated professionals who are recognized as the finest financial investigators in the world.

The Intelligence Unit quickly became renowned for the financial investigative skill of its Special Agents and commenced one of its first narcotics investigations on an opium trafficker in Hawaii in the early 1920s, pursuing the only charge it could—tax evasion. It attained national prominence in the 1930s for the income tax evasion conviction of "Public Enemy Number One," Al Capone, and its role in solving the Lindbergh kidnapping. From these promising beginnings, the Intelligence Unit expanded over the intervening decades, investigating tax evasion by ordinary citizens, prominent businesspersons, government officials, and notorious criminals.

In July 1978, the Intelligence Unit became Criminal Investigation (CI) and its statutory jurisdiction expanded to include money laundering and currency violations in addition to its traditional role in investigating tax violations. However, IRS-CI's core mission remains unchanged. It continues to help ensure the integrity and fairness of the system of taxation in the United States. Since IRS-CI's inception in 1919 to the present, the conviction rate for federal tax prosecutions has never fallen below 90 percent—a record of success that is unmatched in federal law enforcement.

For decades, unreported funds have been laundered through various financial institutions. There would generally be no paper trail within the financial institution other than bank account records, if the money was deposited. Further, there was historically no requirement for banks to report most currency transactions. The BSA, enacted in 1970, authorized the Secretary of the Treasury to issue regulations requiring financial institutions to maintain records and file reports on certain financial transactions. With the enactment of the BSA came the introduction of the Currency Transaction Report (CTR), Report of International Transportation of Currency or Monetary Instruments (CMIR) and Report of Foreign Bank and Financial Accounts (FBAR, Form TD F 90-22.1). As a result of the BSA, currency transactions began to have a family tree—with all the branches firmly and clearly attached.

Thousands of financial institutions are currently subject to BSA reporting and recordkeeping requirements, including depository institutions (*e.g.*, banks, credit unions and thrifts); brokers or dealers in securities; money services businesses (*e.g.*, money transmitters; issuers, redeemers and sellers of money orders and traveler's checks; check cashiers and currency exchangers); and casinos and card clubs. IRS-CI has been able to follow this paper trail to disrupt and dismantle, through investigation, prosecution and forfeiture of assets, many criminal organizations failing to appropriately report their income or otherwise involved in criminal activity.

IRS Anti–Money Laundering Programs

Each year, billions of dollars in unreported funds are laundered through banks and nonbanking financial institutions, such as money servicing businesses, in an effort to make the money appear legitimate or to evade taxes. The IRS's Anti–Money Laundering team coordinates its efforts with all affected governmental agencies to identify, detect and deter money laundering in furtherance of tax evasion, a criminal enterprise, terrorism, tax evasion or other unlawful activity.

An effective tool for documenting financial crime has been information obtained from banks and other nonbanking financial institutions. The family tree of currency transactions began to spread its roots beyond the BSA (1970) with the Anti-Drug Abuse Act of 1986[2] (which had substantive amendments to Title 31) and the USA PATRIOT Act in 2001.[3] These Acts require banks and other financial institutions to become even more involved in solving financial crimes by filing various reports with the government including CTRs and SARs. The IRS conducts ongoing outreach efforts with the banking industry and nonbanking financial institutions to ensure awareness with the money laundering statutes. The IRS has created relationships across the financial sector and with other federal and state authorities to combat abusive tax schemes, terrorist financing and money laundering.

Since September 11, 2001, the IRS has increased its anti–money laundering activities by creating the IRS-CI Counterterrorism Section that focuses investigative efforts on money laundering activities potentially associated with terrorist financing. IRS Special Agents have been assigned to the Joint Terrorism Task Forces. In addition, the IRS SB/SE's Anti–Money Laundering groups search for compliance with the registration, reporting and record-keeping requirements of the money laun-

dering statutes. The IRS also has the authority to enforce the reporting and record-keeping requirements related to the Report of Foreign Bank and Financial Accounts (FBARs) in looking into offshore accounts used for money laundering which often includes the concealment of assets and income tax evasion.

IRS-CI: Electronic Crimes Program

The financial investigators of IRS-CI fill a unique niche in the federal law enforcement community. Sophisticated schemes and the complex American economy demand the analytical ability of financial investigators to filter complex arrays of financial records. Records of transactions have generally moved from simple paper ledgers to computers to offsite, online storage to someplace in the electronic cyberspace. IRS-CI is continually developing techniques to locate and retrieve electronic records located throughout the world.

IRS-CI designed the Electronic Crimes Program (ECP) to exploit its expertise in computer and network forensics. As the incidence of computers discovered during enforcement actions has increased from five percent to 95 percent, the reliance on ECP personnel to secure and analyze digital data has similarly increased. Previously, government agents might find a single personal computer; now they encounter multiple computers, often linked together in a complex network, each having the capacity to store vast quantities of documents.

Computer Investigative Specialists (CISs) participate in the execution of search warrants and use specialized equipment and techniques to preserve digital evidence and to recover financial data, including data that may have been encrypted, password protected or otherwise electronically disguised. Their primary mission is to secure the data, reduce it by eliminating programs and other files of nonevidentiary value and then provide the critical information to the investigating agent. The agent can then electronically review evidence, which is significantly more efficient than historical manual paper procedures. This technique, together with the scanning of paper documents, puts the entire investigation in a digital format that allows the investigation team and prosecutors to locate items of interest, transfer files among themselves and digitally present evidence in the ever-emerging electronic courtrooms throughout the country.

Data Input and Research Facilities

IRS-CI's agents are proficient with both new computers and software and data technology that may still be used in financial crimes. The ECP Data Input Center in Kentucky is a sophisticated scanning and transcription center capable of converting volumes of paper evidence into a searchable digital format. An ECP research and training facility in Virginia focuses on developing and enhancing techniques for processing digital evidence, using cutting-edge technology, coordinating existing technology and training CISs. These facilities enable agents across the country and around the world to electronically follow a target into cyberspace to locate evidence of a financial crime.

ILOOK©

IRS-CI often obtains information others thought was long ago deleted and forgotten. IRS-CI and other federal agencies developed ILOOK©, a forensic software tool that automates the hard drive analysis process and makes it possible for a CIS to quickly review the multi-gigabyte drives contained in modern computers. The Linux-based ILOOK© Imager allows the CIS to image almost any computer they encounter, including mass data storage systems and non-Microsoft operating systems. ILOOK© is supported by the FBI and NASA and is freely distributed to other federal, state and local law enforcement agencies. This information is obtained at the business site during execution of the search warrant within several hours—less if the company's system administrator is allowed to assist IRS-CI (which may be preferable to a longer presence by IRS-CI representatives on the business premises).

ILOOK© recovers exact searchable copies of all data (including deleted files) from the target drive image and assists the investigative search for specific details and allows the insertion of foreign language character sets to search for information. ILOOK© provides the case agent with a working copy of the target's computer information. Counsel should request a copy of the image obtained by IRS-CI through ILOOK© as soon as possible after the execution of a search warrant and they should obtain an image directly from the business. Since businesses often continue to use their computers following a search, they may change and update relevant information. Counsel must be aware of the information being analyzed by IRS-CI from the computers of the business operations.

Financial Crimes Enforcement Network (FinCEN)

The Financial Crimes Enforcement Network (FinCEN) was established in April 1990 to provide a government-wide, multi-source intelligence and analytical network to support the detection, investigation and prosecution of domestic and international money laundering and other financial crimes. In May 1994, its mission was broadened to include various regulatory responsibilities.

FinCEN oversees and implements policies to prevent and detect money laundering throughout the world using anti–money laundering statutes (such as the BSA) which require reporting and record-keeping by banks and other financial institutions. FinCEN also provides intelligence and analytical support to other law enforcement authorities. FinCEN concentrates on combining information reported under the BSA with other government and public information which is then disclosed in the form of intelligence reports to the law enforcement community. These reports assist ongoing investigations and help plan future money laundering investigative strategies.

Money laundering is a worldwide problem for FinCEN. Through Project Gateway, FinCEN provides online access to BSA information to assist law enforcement officials in each state, the District of Columbia and the Commonwealth of Puerto Rico with their anti-money laundering and financial crimes investigations. Gateway's technology provides direct electronic access to critical financial information saving investigative resources since subscribing agencies perform their own research on the system. Information on incoming inquiries is automatically compared with prior inquiries enabling the coordination of federal and state agencies having similar interests. Automated reports—Gateway Alerts—containing the index-level data and contact points are provided to each agency having an interest allowing the coordination of investigations and the sharing of intelligence. FinCEN's analysts provide case support to more than 165 federal, state and local agencies, issuing approximately 6,500 intelligence reports each year.

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FinCEN is an international leader in the attack on financial crimes and the corresponding corruption of international economies. FinCEN coordinates with financial intelligence units (FIUs) in scores of countries, including Britain, France, Belgium and Australia, and is assisting the establishment of worldwide FIUs.

Currency Reporting Requirements

The Currency Transaction Report (CTR) came into existence with the passage of the Currency and Foreign Transactions Reporting Act,[4] better known as the BSA, in 1970. However, by 1975, only 3,418 CTRs had been filed in the United States. Due to the concern by financial institutions about the Right to Financial Privacy, when the CTR was initially introduced, questionable transactions of less than $10,000 were only reported to the government if a suspicious bank teller called an agent and provided the information. On October 26, 1986, with the enactment of the Money Laundering Control Act,[5] the Right to Financial Privacy was no longer an issue. As part of this Act, financial institutions could not be liable for releasing suspicious transaction information to law enforcement authorities. As a result, CTRs were revised to include a "check box" for suspicious transaction (which remained in effect until April 1996 when the SAR was introduced).

There are different reporting requirements for different types of transactions and financial institutions as well as nonfinancial institutions. Most reports are filed electronically and coordinated at the IRS Detroit Computing Center in Michigan (although many can be hand-delivered to a local IRS office) and are entered into the Currency and Banking Retrieval System (CBRS) creating an electronic roadmap for investigations of financial crimes and illegal activities, including tax evasion, embezzlement, and money laundering. Reports are to be entered into the CBRS within 30 days following their receipt, and much of this data can be accessed by federal, state and local law enforcement agencies (subject to disclosure restrictions) for at least 10 years thereafter. Currency forms, their reporting requirements, and the number filed in calendar year 2003 include the following:

Currency Transaction Report (CTR), FinCEN Form 104 (replaced IRS Form 4789 effective December 1, 2003). The CTR must be filed by financial institutions engaging in a currency transaction in excess of $10,000. Each financial institution (other than casinos, which must instead file FinCEN Form 103 CTRC) must file Form 104 (CTR) with respect to any deposit, withdrawal, exchange of currency or other payment or transfer, by, through or to the financial institution that involves a currency transaction of more than $10,000. Multiple transactions must be treated as a single transaction if made by or on behalf of a single person and if they result in either currency received or disbursed (without offset) by the financial institution totaling more than $10,000 during any single business day. The CTR must be filed with the IRS Detroit Computing Center within 15 days after the transaction. The term "currency" includes coins and paper money of the United States or any other country. The failure to file a CTR, failure to supply information or filing a false or fraudulent CTR is subject to various civil and criminal penalties set forth in 31 USC §§5321, 5322 and 5234. *CTRs filed in calendar year 2003: 12,506,035.*

Currency Transaction Report Casino (CTRC), FinCEN Form 103, FinCEN Form 103-N for Nevada Casinos (replaced IRS Forms 8362 and Form 8852). The CTRC must be filed by a casino to report currency transactions aggregating in excess of $10,000 in a gaming day within 15 days after the transaction. Each casino must file FinCEN Form 103 (FinCEN Form 103-N for Nevada casinos) with the IRS Detroit Computing Center for each deposit, withdrawal, exchange of currency or gambling tokens or chips, or other payment or transfer, by, through or to such casino which involves aggregate transactions in currency of more than $10,000. Civil and/or criminal penalties may be assessed for the failure to file a CTRC or supply information or for filing a false or fraudulent CTRC are set forth in USC §§5321, 5322 and 5324. *CTRs filed in calendar year 2003: 451,457.*

Report of Foreign Bank and Financial Accounts (FBAR) Treasury Form TD F-90.22.1. The FBAR must be filed by individuals to report a financial interest in or signatory authority over one or more accounts in any foreign country. Each U.S. person who has a financial interest in, or signature authority over, any financial account including bank, securities or other types of financial accounts, in a foreign country must report that relationship by filing an FBAR if the aggregate value of these financial accounts exceeds $10,000 at any time during the calendar year. FinCEN delegated authority to assess FBAR penalties to the IRS. The deadline to file the FBAR with the Department of the Treasury in Detroit, Michigan, for each calendar year is on or before June 30 of the following year. The term "U.S. person" includes a citizen or resident of the United States, domestic partnership, domestic corporation or a domestic estate or trust. Criminal penalties for the failure to file the FBAR or to supply information or for filing a false or fraudulent FBAR are set forth in 31 USC §§5321, 5322 and 5324. *FBARs filed in calendar year 2003: 202,030.*

IRS/FinCEN Form 8300, Report of Cash Payments Over $10,000 Received in a Trade or Business. Form 8300 must be filed by persons engaged in a trade or business who, in the course of that trade or business, receive more than $10,000 in cash in one transaction or two or more related transactions within a 12-month period. The term "cash" includes U.S. and foreign coin and currency and for a designated reporting transaction (retail sale of a consumer durable having a useful life of at least one year; collectibles—art, rugs, antiques, *etc.*; or a travel or entertainment activity) cashier's checks, money orders, bank drafts and traveler's checks. Transactions are related if they occur within 34 hours or if the recipient knows or has reason to know each transaction is part of a series of connected transactions. Form 8300 must be filed with the IRS Detroit Computing Center within 15 days of the cash payments aggregating more than $10,000, but need not be filed in a transaction occurring entirely outside the United States or in a transaction that is not in the course of a person's trade or business. The recipient of the cash must provide the payor with a statement by the following January 31 indicating that a Form 8300 was filed with respect to the underlying transaction. *Forms 8300 filed in calendar year 2003: 129,816.*

Suspicious Activity Report (SAR) Treasury Form TD F-90.22.47. Financial institutions operating in the United States, including insured banks, savings associations, savings association service corporations, credit unions, bank holding companies, non-bank subsidiaries of bank holding companies, Edge and Agreement corporations and U.S. branches and agencies of foreign banks are required to file an SAR where they know of, suspect, or have reason to suspect insider abuse involving any amount, violations

aggregating $5,000 or more where a suspect can be identified, violations aggregating $25,000 or more regardless of a potential suspect, or transactions aggregating $5,000 or more that involve potential money laundering or any violation of the Bank Secrecy Act. SARs must also be filed when transactions are structured as part of a plan to violate federal laws and financial reporting requirements (*e.g.*, classic structuring transactions). *SARs filed in calendar year 2003: 285,814.*

Suspicious Activity Report Casino (SARC) FinCEN Form 102 (previously TD F-90.22.49). SARCs must be filed with respect to transactions or attempted transactions conducted or attempted by, at, or through a casino, involving or aggregating at least $5,000 in funds or other assets where the casino/card club knows, suspects or has reason to suspect that the transactions or a pattern of similar transactions involve funds potentially derived from illegal activities. SARCs must also be filed when transactions are part of a plan to violate federal laws and transaction reporting requirements (*e.g.*, classic structuring transactions). *SARCs filed in calendar year 2003: 5,016.*

Registration of Money Services Business (RMSB) Treasury Form TD F-90.22.55. Each "money services business," except one that is a money services business solely because it serves as an agent of another money services business, must register by filing form TD F 90-22.55.[6] *RMSBs filed in calendar year 2003: 14,226.*

Suspicious Activity Report by Money Services Businesses (MSB) (SARM) Treasury Form TD F-90.22.56. SARMs must be filed within 30 days of becoming aware of transactions or attempted transactions conducted or attempted by, at or through an MSB, involving or aggregating funds or other assets of at least $2,000 in funds or other assets where the MSB knows, suspects or has reason to suspect that the transactions or a pattern of similar transactions involve funds potentially derived from illegal activities. SARMs must also be filed when transactions are part of a plan to violate federal laws and transaction reporting requirements (structuring) or when the transaction has no business or apparent lawful purpose and the MSB knows of no reasonable explanation for the transaction following an examination of the available facts. When transactions are identified from a review of records of money orders or traveler's checks that have been sold or processed, an issuer of money orders or traveler's checks is required to report a transaction or a pattern of similar transactions that involves or aggregates funds or other assets of at least $5,000. *SARMs filed in calendar year 2003: 200,919.*

Suspicious Activity Report by the Securities & Futures Industries—FinCEN Form 101. Form 101 must be filed with respect to transactions or attempted transactions conducted by, at, or through a broker-dealer, involving aggregates funds or other assets of at least $5,000 where the broker-dealer knows, suspects or has reason to suspect that the transaction involves funds potentially derived from illegal activities or intended or conducted in order to hide or disguise funds or assets derived from some illegal activity. Forms 101 must be filed when transactions are designed, whether through structuring or other means, to evade filing requirements. They must also be filed when the transaction has no business or apparent lawful purpose or is not the sort in which the particular customer would normally be expected to engage, and the broker-dealer knows of no reasonable explanation for the transaction following an examination of the available facts. Form 101 must also be filed when the transaction involves the use of the broker-dealer to facilitate criminal activity. *Forms 101 filed in calendar year 2003: 4,267.*

Designation of Exempt Person Treasury Form TD F-90.22.53. These forms are used by banks or other depository institutions to designate eligible customers as exempt persons from currency transaction reporting rules (mostly regular business customers with routine needs for currency). Forms *TD F-90.22.53 filed in calendar year 2003: 63,101.*

Report of International Transportation of Currency or Monetary Instruments—FinCEN Form 105 (Formerly Customs Form 4797) if funds are accompanied by an individual; FinCEN Form 106 if funds are mailed, shipped or received. Each person who physically transports, mails, ships or causes to be physically transported, mailed, shipped or received currency or other monetary instruments in an aggregate amount exceeding $10,000 on any one occasion from the United States to any place outside the United States, or into the United States from any place outside the United States must file FinCEN Form 105 (CMIR) or FinCEN Form 106. The term "monetary instruments" includes coin or currency, traveler's checks in any form, negotiable instruments (checks and notes) in bearer form, endorsed without restriction, made out to a fictitious payee or otherwise in a form where title passes upon

delivery; signed incomplete instruments where the payee is omitted; and bearer stock or securities. Recipients of mailed currency must file the report within 15 days with the Customs Officer in charge at any port of entry or with the Commissioner of Customs in Washington, D.C.; shippers must file the report with the Commissioner of Customs on or before the date of mailing or shipping; travelers must file the report at the time of entry to or departure from the limited status with the Customs Officer in charge. Civil and criminal penalties, including the possible seizure and forfeiture of the funds involved are set forth in 31 USC §5321 and 31 CFR 103.57; 31 §USC 5322 and 31 CFR 103.59; 31 USC §5317 and 31 CFR 103.58; and 31 USC §5322. *Forms 105/106 filed in calendar year 2003: Not applicable.*

Other industries are required to file Suspicious Activity Reports as well. The U.S. Department of Treasury's Financial Crimes Enforcement Network provides additional information regarding the reporting requirements at *www.fincen.gov* and forms are available at *www.msb.gov* together with *www.irs.gov.*

USA PATRIOT Act

On October 26, 2001, President Bush signed into law the United and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 ("the PATRIOT Act"). The PATRIOT Act added enhanced money laundering provisions to Chapter 53 of Title 31 of the United States Code. Many of these provisions also have implications for tax investigative and tax withholding purposes.

Qualified Intermediary Provisions

The Qualified Intermediary (QI) provisions require a QI to provide the identity of the beneficial owner and the production of documents if certain new money laundering provisions apply, notwithstanding foreign bank secrecy laws. Another provision has the potential for requiring all foreign persons who open or maintain an account in the United States to obtain an identifying number. This legislation clearly raises issues about potential conflicts with foreign bank secrecy laws that impose civil or even criminal sanctions on the release of confidential information about an account holder.

Payable Through or Correspondent Account Provisions

A foreign financial institution that opens or maintains a "payable-through" (an account through which a foreign financial institution allows its customers to engage in usual banking activity) or correspondent account with a domestic financial institution or agency as a condition to opening or maintaining account must (1) identify each customer of the foreign financial institution who is permitted to use, or whose transactions are routed through, the account and (2) obtain information about those customers that is "substantially comparable" to information that must be obtained about U.S. customers.

Know Your Customer Procedures Provision

Section 5318(l) of Title 31 mandates the application of "Know Your Customer" (KYC) procedures for U.S. financial institutions. Under such rules, a U.S. financial institution must verify the identity of an account holder and maintain records of the information used to verify the account holder's identity.

U.S. Account Maintained by Foreign Persons Provision

Another special measure would permit the Treasury to require a domestic financial institution to obtain information about the beneficial owner of any account opened or maintained in the United States by a foreign person.

Summons Authority Over Foreign Bank Records Provision

The PATRIOT Act adds a new subsection to Section 5318 of Title 31 that authorizes either the Treasury or the Justice Department to issue a summons or subpoena to a foreign bank that maintains a correspondent account in the United States for records maintained by the bank (including records maintained outside the United States) that relate to the U.S. correspondent account. The foreign bank must respond to the summons request within seven days of receipt of the summons request. This provision is comparable to the summons provision under Code Sec. 6038A(e)(1) that permits the IRS to obtain records with respect to a U.S.-connected transaction maintained outside the United States by a foreign person related to a foreign-owned U.S. corporation.

Offshore Voluntary Compliance Initiative (OVCI)

On January 15, 2003, the IRS issued a news release (IR-2003-5)[7] and revenue pro-

cedure (Rev. Proc. 2003-11)[8] unveiling a compliance initiative aimed at bringing taxpayers who used "offshore" payment cards or other offshore financial arrangements to hide their income, back into compliance with the tax laws. This revenue procedure applied to tax years ending after December 31, 1998, and to tax years ending before that date to the extent provided in the revenue procedure. The deadline for filing a request to participate in the OVCI was April 15, 2003.

With respect to unreported income or false deductions associated with the use of offshore payment cards or offshore financial arrangements, through OVCI the IRS agreed not impose civil fraud penalties under Code Sec. 6663, fraudulent failure to file penalties under Code Sec. 6651(f) or information return civil penalties under the relevant Code sections. In appropriate circumstances, the IRS would impose delinquency penalties and the accuracy-related penalty. FinCEN agreed not to impose civil penalties for failure to timely file an FBAR. The IRS treated the request to participate in the OVCI as a request to make a voluntary disclosure.

According to the July 21, 2004, testimony of Michael Brostek, Director of the U.S. Government Accountability Office before the Senate Committee on Finance, of more than one million taxpayers estimated by IRS to be involved in an offshore scheme, the IRS only received OVCI Applications from 1,321 taxpayers (including seven deceased applicants and 400 entities set up by the applicants to handle the offshore funds) from 47 states, the District of Columbia and 48 countries. All but 16 applied for relief for at least tax years 1999, 2000 and 2001, and half of all OVCI applications were received from Florida, California, Connecticut, Texas, and New York. Florida led with 141 applicants, followed by California with 115, Texas with 71, and New York with 47. The IRS rejected 49 applications for a failure to divulge the entirety of the offshore involvement (less than 16 percent of all OVCI applicants for tax year 2001 said they used a "promoter"—as the term was defined in the application—although 93 percent said that a paid preparer prepared their 2001 original return). The applications covered more than 3,500 tax years and included at least $200 million in tax, penalties and interest. A number of the applications involved taxes exceeding $1 million. In the first 229 OVCI cases reviewed, taxpayers identified 107 different offshore promoters. Of these, the IRS identified 80 new promoter cases, which carry significant potential for future agency efforts to track down offshore tax evaders. Further, there was a significant "year-to-date" increase in the filing of amended returns with IRS Service Centers during the term of the OVCI.

Organization for Economic Cooperation and Development (OECD)

"Tax havens" have flourished over the last 20 years. The International Monetary Fund has estimated that assets worth more than $5 trillion are held in offshore tax havens. Governments have a duty to protect their interests in the face of those who use tax havens to avoid their legal obligations to pay taxes in their countries of residence. In support of that obligation, the OECD publishes a *List of Uncooperative Tax Havens*. Uncooperative tax havens threaten the tax systems of developed and developing countries and also the integrity of the international financial system.

More than 30 offshore financial centers have pledged to work with OECD countries to counter harmful tax practices. Former "tax haven" countries participating in the OECD have pledged to eliminate their own harmful tax practices. Cooperating countries include Anguilla, Antigua, Aruba, Bahamas, Bahrain, Belize, British Virgin Islands, Cook Islands, Gibralter, Grenada, Guernsey, Isle of Man, Jersey, Montserrat, Netherlands Antilles, Niue, Nevis, Panama, St. Kitts, Seychelles, and the U.S. Virgin Islands. These countries have agreed to provide transparency in accounting standards and with regard to the ownership of companies, and a willingness to exchange information with other countries. OECD member countries permit access to bank information, directly or indirectly, for all tax purposes so that tax authorities can fully discharge their revenue raising responsibilities and engage in effective exchange of information with their treaty partners. OECD member countries further agree to eliminate anonymous accounts and require identification of bank customers and beneficial owners of accounts.

The OECD aims to foster economic growth and development and ensure efficient and equitable flow of capital world-wide by

promoting fair competition on tax rates. By getting commitments from more than 30 offshore financial centers to cooperate in fighting harmful tax practices, the OECD is attempting to protect the tax base of OECD countries and of developing countries. By promoting transparency and cooperative agreements between all economies, OECD's work contributes to efforts to counter money laundering and the financing of terrorism (and strengthen the international financial system) maintained by the bank (including records maintained outside the United States) that relate to the U.S. correspondent account. The foreign bank must respond to the summons request within seven days of receipt of the summons request. This provision is comparable to the summons provision under Code Sec. 6038A(e)(1) that permits the IRS to obtain records with respect to a U.S.-connected transaction maintained outside the United States by a foreign person related to a foreign-owned U.S. corporation.

Reporting Suspected Tax Fraud

Reports of suspected tax fraud can be made by phone, mail or at a local IRS walk-in office. Contact can occur by phone to the IRS toll free at 1-800-829-0433. International callers may call their U.S. Embassy or call 215-516-2000 (not a toll-free number). Contact can occur by mail to the IRS Service Center where tax returns are filed. Informants are not required to provide their identity and their identity can be kept confidential. Informants may also be entitled to a reward.[9] For those living outside the United States, the IRS has full-time permanent staff in seven U.S. embassies and consulates.

Show Me the Money!

Individuals often underestimate the ability and resourcefulness of the government. The events of September 11, 2001, enhanced the government's already strong desire to ensure the reporting of monetary transactions within the United States. The focus on terrorism provided a wealth of information to the government and brought a spotlight to many transactions that otherwise would have entirely escaped detection. Those who choose not to comply face potentially significant civil and criminal sanctions that should not be ignored. Big Brother has arrived ... with a lot of friends and a tool chest full of creative ideas, desire and electronic information-gathering techniques each designed to "show me the money!"

ENDNOTES

1 Bank Secrecy Act of 1970 (P.L. 91-508).
2 Anti-Drug Abuse Act of 1986 (P.L. 99-570).
3 United and Strengthening America by Providing Appropriate Tools Required to Intercept and Obstruct Terrorism Act of 2001 (P.L. 107-56).
4 *Supra* note 1.
5 *Supra* note 2.
6 *See* 31 CFR 103.11(n) and (uu) for definitions of money services businesses.
7 IRS News Release, IR-2003-5, Jan. 14, 2003.
8 Rev. Proc. 2003-11, IRB 2003-4, 311, 2003-1 CB 311.
9 *See* IRS Publication 733.