



Coming Attractions: 2023 IRS Civil and Criminal Tax Enforcement Priorities

February 8, 2023

Don Fort, Director of Investigations Kostelanetz LLP

As Chief of IRS-CI from 2017 to 2020, Don led the sixth largest U.S. law enforcement agency, managing a budget of over \$625 million and a worldwide staff of approximately 3,000, including 2,100 special agents in 21 IRS field offices and 11 foreign countries. Don modernized IRS-CI by developing cutting-edge, data-centric methods of detecting criminal non-compliance through algorithms and other models. He also significantly expanded IRS-CI's capabilities in cyber-crime and cryptocurrency investigations and expanded the agency's international presence and footprint. Don led IRS-CI in identifying and investigating over \$11.5 billion in tax loss and \$14.8 billion in other criminal proceeds.

As both Chief and Deputy Chief of IRS-CI, he oversaw numerous high-profile matters, including the college admissions scandal known as "Varsity Blues" that ensnared several celebrities; the Paul Manafort and Michael Cohen federal tax investigations; the Michael Avenatti tax investigation; the takedown of the largest darknet child exploitation website funded by cryptocurrency; two Chinese nationals who were charged with laundering \$100 million in the hack of a cryptocurrency exchange; the Swiss Bank Program in which 80 Swiss banks entered into agreements with the government and paid \$1.36 billion in penalties; the Federation Internationale de Football Association (FIFA) worldwide money laundering, structuring, and tax evasion matter; the Credit Suisse guilty plea, and many more. Don graduated from Gettysburg College with a B.A. in Management in 1990 and is licensed as a CPA in the Commonwealth of Virginia.



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Caroline D. Ciraolo, former Acting Assistant Attorney General of the U.S. Department of Justice's Tax Division, is a partner with Kostelanetz LLP and a founder of its Washington, D.C. office.

Her practice focuses on federal and state civil tax controversies, including representation in sensitive audits, administrative appeals, and litigation, providing related tax advice, conducting internal investigations, and representing individuals and entities in criminal tax investigations and prosecutions. Caroline is President of the American College of Tax Counsel, immediate past Chair of the ABA Tax Section's Civil and Criminal Tax Penalties Committee, and inaugural Vice Chair of Membership, Diversity, and Inclusion of the ABA Tax Section.

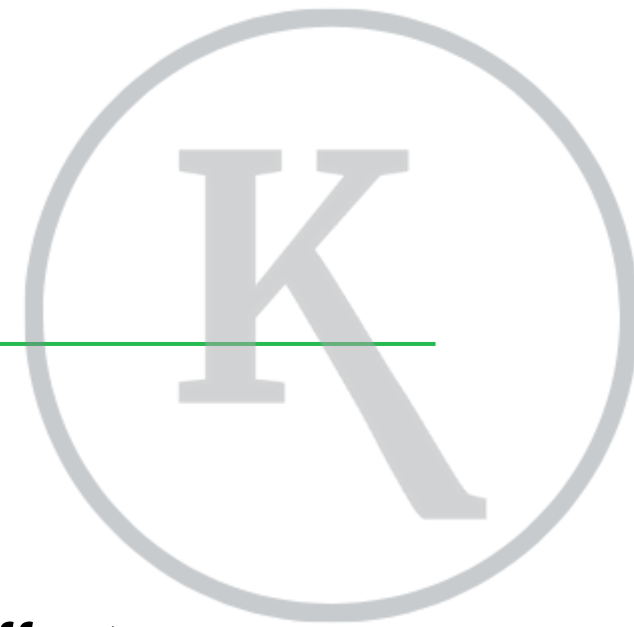
She is a recipient of the IRS Chief Counsel Award and the ABA Tax Section's Janet Spragens Pro Bono Award. Caroline serves as an Adjunct Professor at the Georgetown University Law Center (*Criminal Tax Law & Procedure* and *International Tax Controversies*) and University of Baltimore School of Law Graduate Tax Program (*Investigation, Prosecution, and Defense of Tax Crimes* and *Tax Practice & Procedure*). Caroline has been recognized by Chambers (Band 1, Tax Fraud (nationwide); Band 1 (High Net Worth: Private Client) (nationwide); Band 2, Tax (DC)), Legal 500, International Tax Review, Best Lawyers in America (Lawyer of the Year, Litigation and Controversy – Tax (Washington, D.C.) (2022)), Super Lawyers, and The Daily Record's Top 100 Women Circle of Excellence.



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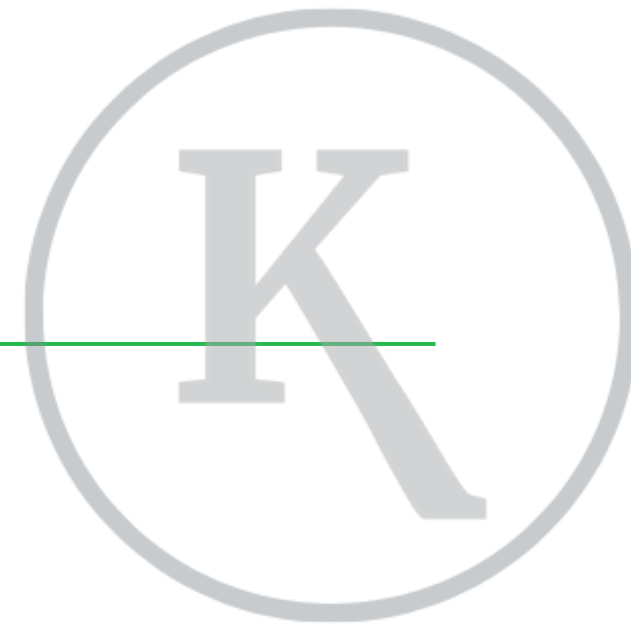
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Agenda



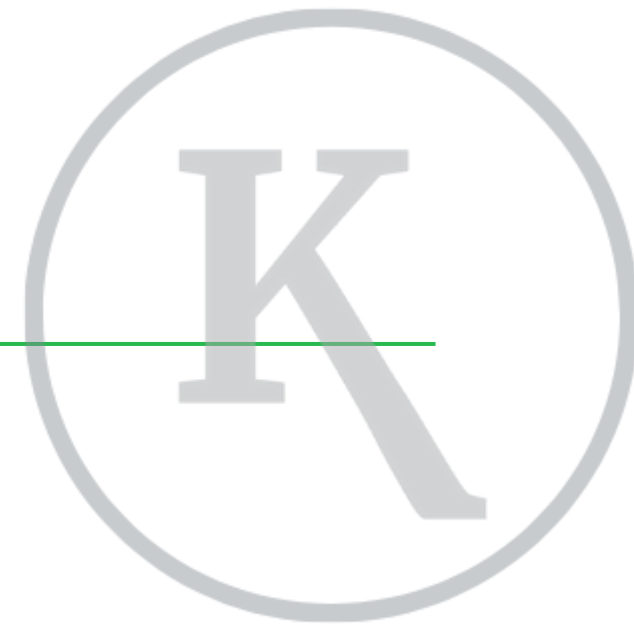
- IRS Dirty Dozen
- IRS Enforcement Priorities
- International and Cryptocurrency Enforcement Efforts
- Parallel Proceedings
- Best Practices

2022 IRS “Dirty Dozen”



1. Use of Charitable Remainder Trust (CRAT) to Eliminate Taxable Gain
2. Maltese (or Other Foreign) Pension Arrangements Misusing Treaty
3. Puerto Rican and Other Foreign Captive Insurance
4. Monetized Installment Sales
5. Pandemic-Related Scams Including Theft of Benefits and Bogus Social Media Posts
6. Offer in Compromise Mills
7. Suspicious communications designed to fool someone into responding before thinking
8. Spear phishing
9. Concealing assets – offshore accounts and improper reporting of digital assets
10. High-income individuals who fail to file
11. Syndicated Conservation Easement Transactions
12. Abusive Micro-Captive Insurance Arrangements

Enforcement Priorities



- High Income Non-filers
- Global High Wealth
- **International Tax Enforcement**
- Micro-captive Insurance
- Syndicated Conservation Easements
- **Virtual Currency**
- Charitable Remainder Annuity Trusts
- Maltese Pension Arrangements
- Improper Monetized Installment Sales
- Research Credit Refund Claims

High Income Non-Filers (HINF)



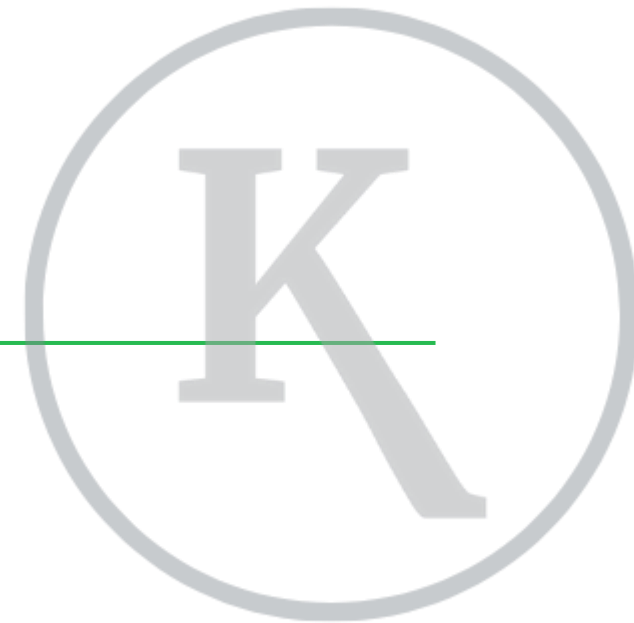
- **TIGTA (Treasury Inspector General for Tax Administration) periodically reviews the IRS's strategy for combatting non-filers**
- Total Tax Gap (2013): \$441 Billion - Non-Filers: \$39 Billion (9%)
- TIGTA Report (May 29, 2020):
 - For TY 2016, number of non-filers exceeded 10 Million
 - As of Dec 2018, 34% of high-income non-filers for TYs 2014 – 2016 (879,415) had not satisfied their filing requirement and represented \$45.7 billion estimated tax due
- Potential Civil Penalties:
 - 26 U.S.C. 6651(a) – failure to timely file and pay penalties (up to 47.5% of tax due)
 - 26 U.S.C. 6651(f) – fraudulent failure to file (up to 75% of the tax due)
- Potential Criminal Charges:
 - 26 U.S.C. 7203 (willful failure to file – misdemeanor)
 - 26 U.S.C. 7201 (tax evasion – felony)

Global High Wealth Enforcement



- Renewed focus on GHW taxpayers
- LB&I Compliance, Planning & Analytics (CP&A) primary responsibility for coordination of Annual Examination Plan and workload identification
- Coordination among LB&I, SB/SE, and TE/GE
- Increased use of data analytics
- Expectation of several hundred audits of high-income taxpayers beginning Fall 2021
- In addition to the “High Income Initiative” – effort by LB&I and SB/SE to maintain compliance efforts with high income taxpayers based on total positive income

Micro-Captive Insurance Schemes



- Businesses form captive insurance companies to insure against risks.
- Insured pays premiums to captive and deducts for premiums paid.
- Captive uses premiums to fund losses incurred by the insured.
- Traditional captive insurance reduces cost of insurance and loss events.
- Micro-captives: Insurers qualifying as small insurance cos. can elect to be treated as exempt organizations or exclude limited annual net premiums from income.
- Micro-captive taxed only on *investment* income. IRC 831(b)
- Some micro-captive promoters, accountants or wealth planners persuade owners of closely-held entities to participate in schemes that lack attributes of insurance.
- Notice 2016-66 (amended by 2017-8) labeled micro-captive insurance arrangements as potentially abusive and required their disclosure to the IRS under threat of penalties.

Micro-Captive Insurance Schemes



2017/2018+	IRS audits/investigations > USTC decisions finding captives did not provide insurance for failure to distribute risk, not acting as insurer commonly would
2019/2020	IRS offers to captive owners – deny 90% of deductions + penalties
2020	IRS sends letters to participants and material advisors IRS formed 12 micro-captive exam teams
2021	IRS News Release 2021-82 (warning to exit transactions) <i>Caylor Land & Dev.</i> , T.C. Memo. 2021-30 <i>CIC Services</i> , SCOTUS (authorizing challenge to 2016-66) <i>DE Department of Insurance</i> , DDE (enforcing IRS summons) <i>Puglisi</i> , USTC (accepted IRS concessions, no merits decision)
2022	<i>Mann Construction</i> , 6th Cir. (Notice 2007-83 declared invalid) <i>CIC Services</i> , EDTN (Notice 2016-66 declared invalid) CCA (non-economic substance microcaptive insurance transactions are adequately disclosed under IRC 6662(i)(2) when material facts are disclosed as reportable on Form 8886, “Reportable Transaction Disclosure Statement,” even if not separately disclosed on Form 8275, “Disclosure Statement”) <i>Moore, Ingram, Johnston & Steele</i> , 11th Cir. (affirmed enforcement of IRS summons issued to law firm regarding management of captive insurance companies) <i>Series Protected Cell 76, A Series of Oxford Ins. Co.</i> , USTC (stipulated decision resulted in \$1 deficiency and no penalty)

Syndicated Conservation Easements



- Charitable contribution deduction generally not allowed for a gift consisting of less than donor's entire interest.
- Exception for “qualified conservation contribution” giving exclusive use for conservation purposes
- Some syndicated conservation easement transactions purport to give investors opportunity to obtain charitable contribution deductions and corresponding tax savings that significantly exceed investment.
- Typically, promoters identify or form a pass-through entity that owns or acquires real property.
- Promoters syndicate (sell) ownership (partnership) interests and advise investors they are entitled to a share of a charitable contribution deduction that greatly exceeds the investment.
- In abusive transactions, promoters obtain inflated appraisals of the easement based on unreasonable factual assumptions/conclusions about development potential.

Syndicated Conservation Easements



Amendments to Section 170(h) included in the Consolidated Appropriations Act, 2023

For easement contributions made by partnerships, the charitable contribution deduction is capped at 2.5 times the sum of each partner's "relevant basis in the partnership."

Exception for long-held (>3 years) property, family partnerships and historic structure easements.

Imposes a new gross valuation misstatement penalty and creates a new strict liability penalty and eliminates Section 6751(b)(2)(A) supervisory approval requirement.

Extends assessment limitations period.

Imposes new reporting requirements.

Requires IRS to publish safe harbor deeds and allows for curing of deed defects in certain cases (limitation defined by reference to transactions described in Notice 2017-10).

Generally effective for charitable contributions made after December 23, 2022 (date of enactment).

Charitable Remainder Annuity Trusts

- Feb. 2022 – U.S. files a complaint in WDMO to prohibit defendants (individuals and entities) from organizing, promoting or selling an allegedly unlawful tax scheme involving the use of CRATs.
- DOJ alleges defendants' involvement with at least 70 CRATs, in scheme that caused estimated \$40 million of unreported taxable income and at least \$8 million in tax loss.
- DOJ alleges that defendants:
 - falsely claimed customers using CRAT scheme can sell property in a way that eliminates the federal tax on the income generated.
 - participates in: (1) convincing customers to contribute property to a CRAT (usually real property that gained value over time); (2) unlawfully inflating (stepping-up) cost basis in the property; (3) selling the property to purchase an annuity; and/or (4) falsely reporting the annuity payments to customers as tax-free distributions of income made by the CRAT.
 - know or have reason to know that statements to customers about tax benefits are false or fraudulent.
- IRS Pubs. 526 and 561: Guidelines for valuing and deducting property donations

U.S.-Malta Income Tax Treaty Abuse



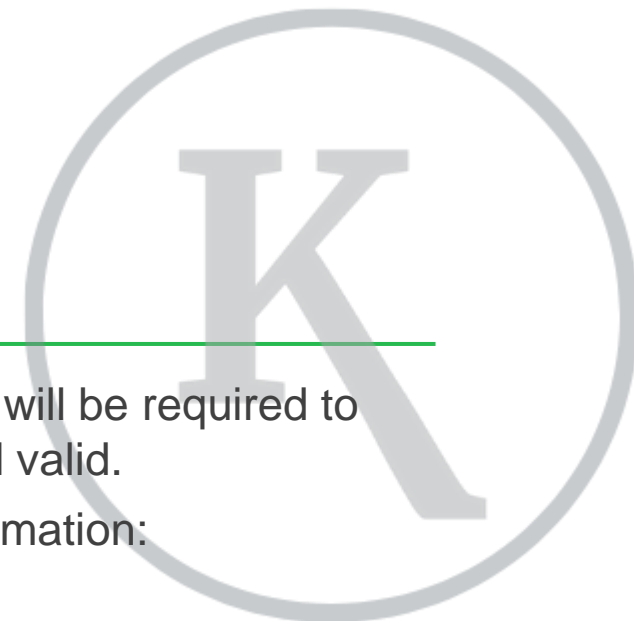
- Treaty signed in 2008 and ratified in 2010 - Art 17 & 18 provide if a resident of one contracting country contributes to a pension plan established under the laws of the other country, then the residence country will not tax the plan's earned income unless and until it would be taxed to a resident of the other country under that country's laws.
- Requirements:
 - Person must be a US resident under Art 4
 - Plan must be a licensed fund under Art 3 ¶ 1(k)
 - Plan must be a pension fund under Art 18 & Art 3 ¶ 1(k)
- USPs interpret this to:
 - Allow unlimited contribution of appreciated property tax-free
 - With no tax due if plan sells property and distributes proceeds to USP
- In 2021, the Paris-based Financial Action Task Force ("FATF"), which monitors countries for their potential to be used by criminal elements for money-laundering and similar purposes, placed Malta on the "grey list" of countries, suggesting a need for greater attention to certain aspects of its financial services and citizenship regimes.
- Dec. 2021 - IRS announces agreement with Malta that Maltese pension plans that allow noncash contributions and unlimited contributions from employment or self-employment will not be considered retirement plans for purposes of the U.S.-Malta income tax treaty

Improper Monetized Installment Sales



- IRS CCA 202118016: M453 transactions (Monetized Installment Sale)
- M453 promoters market the ability to sell an appreciated capital asset, collect the proceeds, and have use of said proceeds, tax-deferred, for 30 years
- Frequent investors are those that are ready for retirement.
- An intermediary purchases appreciated property from seller in exchange for installment note that typically provides payments of interest only, with principal being paid at the end of the term.
- Seller gets lion's share of proceeds but improperly delays gain recognition on the appreciated property until final payment on the installment note, often slated for many years later.
- M453's are complex but generally follow a similar structure. In very limited cases (namely, farm property) they can work, but for virtually all transactions being sold by unscrupulous promoters, the IRS takes the position that they will not withstand scrutiny.
- *Bishop v. IRS (1.9.2023)* – USDC in Utah denied managing director of company promoting monetized installment sales transactions motion to quash IRS summonses seeking information from financial institutions about his and his company's (Slim Ventures, LLC) income.

Research Credit Refund Claims



- Chief Counsel Memorandum 202114101F (Oct. 2021) - Information that taxpayers will be required to include for a research and experimentation credit claim for refund to be considered valid.
- For IRC 41 research credit refund claim, taxpayers must provide the following information:
 - Identify all business components to which the credit relates
 - For each business component, identify all research activities performed and name individuals who performed each research activity, and information each individual sought to discover.
 - Provide total qualified employee wage expenses, qualified supply expenses, and qualified contract research expenses
- **Improper claims** for the research and experimentation credit generally involve failures to participate in, or substantiate, qualified research activities and/or satisfy the requirements related to qualified research expenses.
- IRS issues guidance in Jan. 2022, (LB&I 04-0122-0001), advising IRS personnel procedures to follow to determine if claim is valid
- IRS issues draft instructions for research credit claims (Jan. 10 2023) – Form 6765

The Non-Compliance Spectrum

The Spectrum of Taxpayer Non-Compliance Behaviors

Civil Non-Compliance

Errors
Misunderstanding
Tax Avoidance Planning

Civil Tax Fraud

Aggressive Tax Treatment
First Fraud Indicators
Willfulness

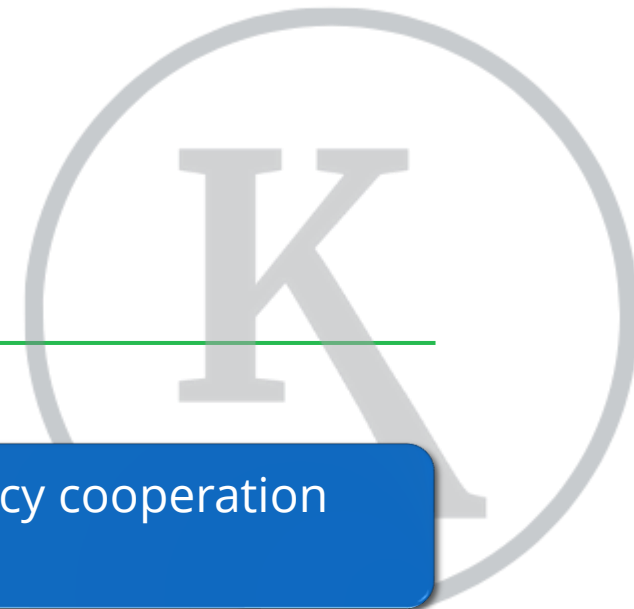
Criminal Non-Compliance

Concealment & Deception
Significant Tax Harm
Firm Fraud Indicators

Pre - IRS Engagement Behaviors

Behaviors During IRS Engagement

IRS Focus on Collaboration and Fraud Awareness



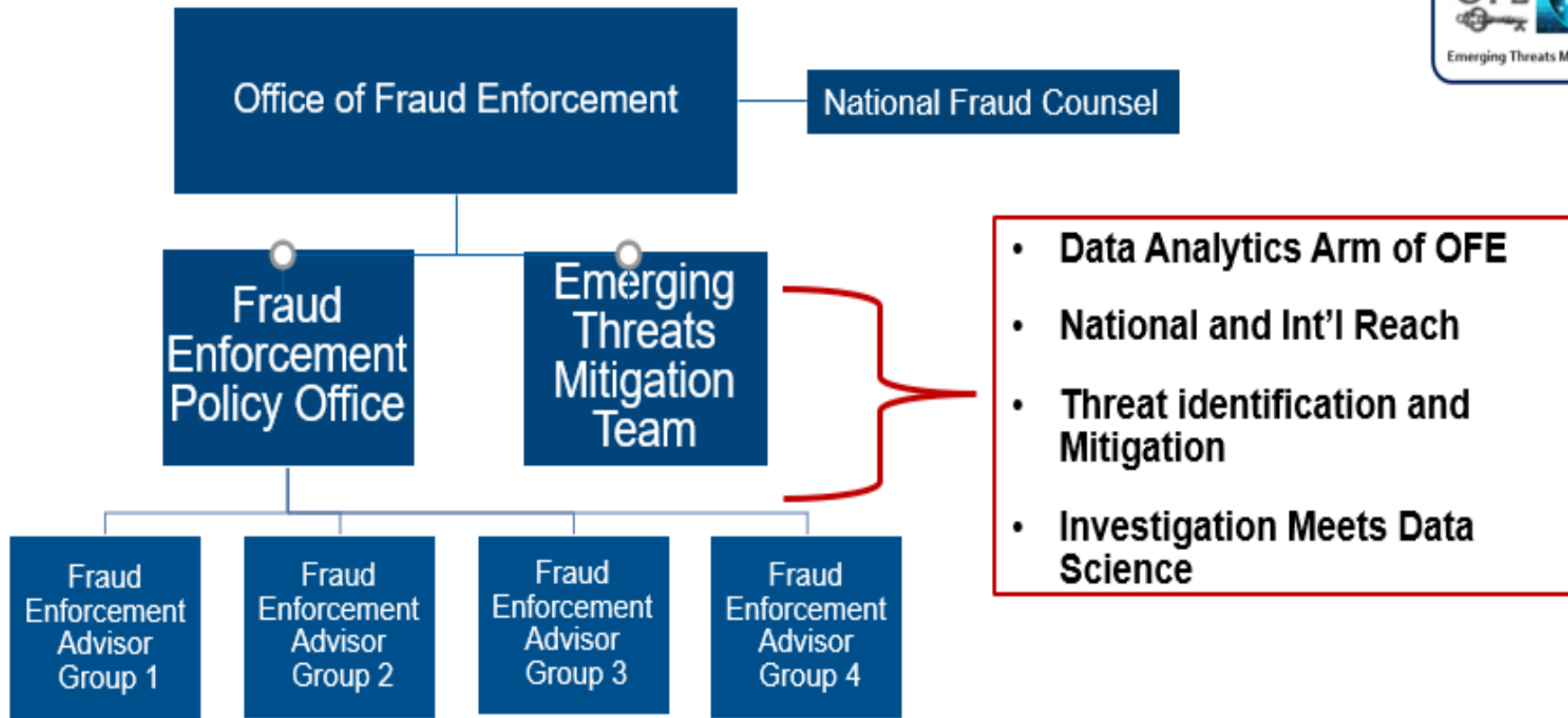
Former Commissioner Charles Rettig brought renewed focus to intra-agency cooperation and collaboration.

Fraud Awareness and Fraud Referrals are a point of emphasis across the agency.

Increasing, the IRS is turning to the use of sophisticated data analytics, data modeling and AI in identifying tax non-compliance.

The priorities and campaigns of one IRS Operating Division are likely complementary across Operating Divisions (Example: Cryptocurrency, Syndicated Conservation Easements)

Office of Fraud Enforcement



Examination and Collection Field Support for Fraud Identification and Development

Criminal Fraud Referrals Within IRS

- Information acquired during a civil examination or a collection proceeding that is provided to IRS Criminal Investigation (CI) from another IRS business operating division (BOD) after affirmative acts (firm indications) of fraud are established and criminal criteria is met.
- Firm indications are defined in Internal Revenue Manual (IRM) 25.1.1 (see IRM 25.1.1.3(2), Indicators of Fraud vs. Affirmative Acts of Fraud).
- Chief of CI stated in December 2021 that CI has received enforcement recommendations against particular taxpayers and suggested areas of potentially criminal noncompliance, with the largest group involving employment tax issues and high-income nonfilers.

IRS CI: Yesterday, Today, and Tomorrow



Yesterday

- ❑ In 1919, the IRS Intelligence Unit was created to investigate widespread allegations of tax fraud.
- ❑ Elmer Lincoln Irey named first Chief, IRS Intelligence Unit.
- ❑ IRS Intelligence Unit quickly became renowned for the financial investigative skill of its special agents.
- ❑ Since its inception, CI has routinely been called upon to investigate the nation's most pressing law enforcement priorities including organized crime, drug cartels, and public corruption.
- ❑ CI played prominent role in some of the most significant and high profile investigations in history.
 - ❑ Al Capone, “public enemy number one,” was convicted on charges of income tax evasion.
 - ❑ Played key role in solving the Lindbergh baby kidnapping.

Today

- ❑ Over the years CI's statutory jurisdiction expanded to include money laundering and currency violations.
- ❑ CI conducts financial investigations worldwide, playing a key role in combating tax fraud, terrorist financing, transnational organized crime, public corruption, and cyber crimes.

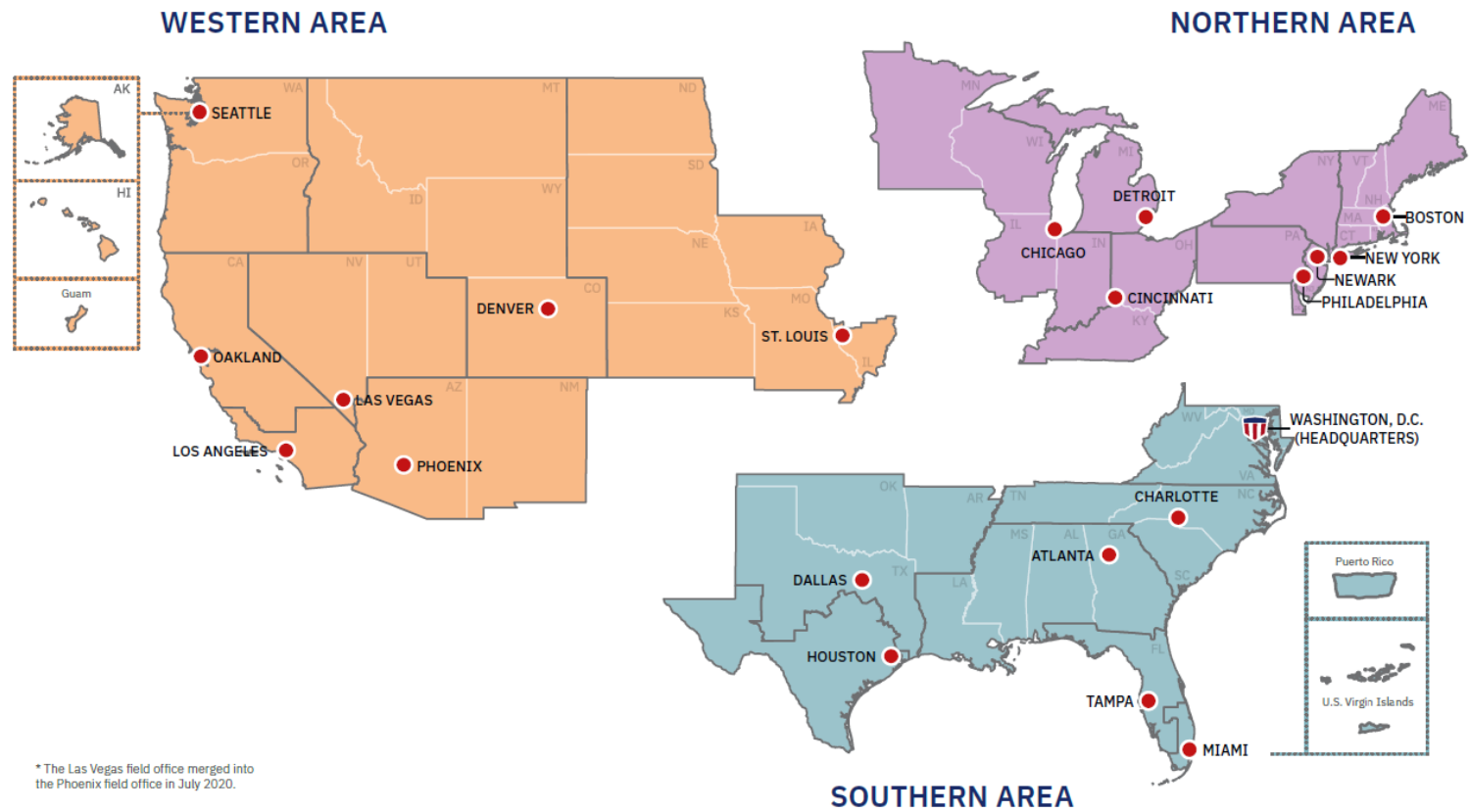
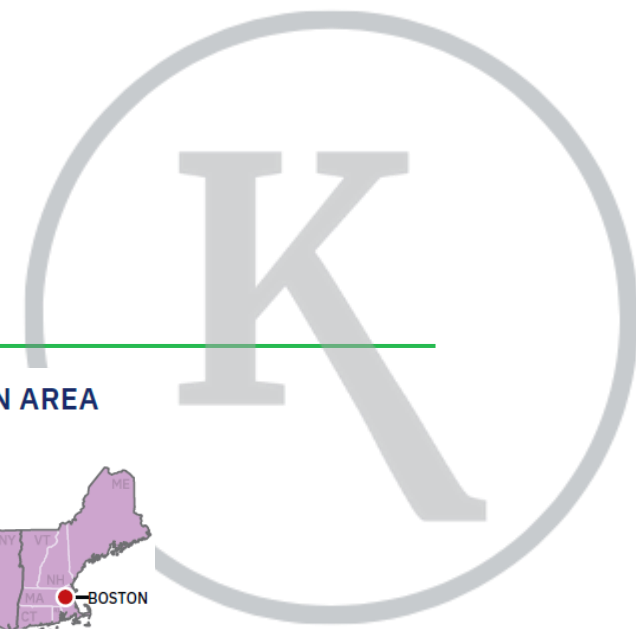
Tomorrow

- ❑ Data analytics tools continue to be a high-priority investment for CI. Connecting the dots in seconds rather than weeks creates efficiencies for our agency (NCIU).
- ❑ Our Cyber Crime enforcement capability is being enhanced to combat criminals sitting at their computers, wreaking havoc on others through the darkweb, and electronically attacking the tax infrastructure.
- ❑ IRS-CI leads some of the most sophisticated cyber-crimes investigations worldwide.

Criminal Enforcement Priorities

Investigative Priority	Case Examples	Highlights
GENERAL FRAUD	Bill Melot – New Mexico Farmer	Sentenced to 14 years in prison for tax evasion and program fraud; Ordered to pay restitution to IRS of \$18.4 million
RETURN PREPARER FRAUD	Gladstone & Jacqueline Morrison	Sentenced to 187 months each; Order to pay nearly \$18 million on restitution
ABUSIVE TAX SCHEMES	Credit Suisse	Guilty plea - conspiracy to aid U.S. taxpayers in filing false returns; agreed to pay \$2.6 billion
	Bank Julius Baer	Deferred Prosecution Agreement and admitted to helping US taxpayers file false tax returns; \$547 million restitution
EMPLOYMENT TAX FRAUD	Tammy Devier	Sentenced to 60 months and convicted of Failure to Pay Over Employment Taxes
CYBER CRIMES AND VIRTUAL CURRENCY	Liberty Reserve and Silk Road; Bitconnect, Bitclub, Twitter Hack	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
TERRORIST FINANCING	Jimenez and Robertson; Hamas, Al Qaeda ISIS COVID-related scams	Guilty of filing false returns to fund travel to Syria; COVID fraud to fund terrorist activity
PUBLIC CORRUPTION	Kwame Kilpatrick	Detroit Mayor Sentenced to 336 months
TRANSNATIONAL ORGANIZED CRIME	FIFA	Uncovered widespread corruption in international soccer. Forty-two subjects charged to date. Restitution exceeds \$190 million
FRIVOLOUS ARGUMENTS	Ronald Joling	Sentenced to 97 months for obstructing the IRS; Restitution of \$1.2 million
ORGANIZED CRIME DRUG ENFORCEMENT TASK FORCES	Edgar Manual Valencia Ortega – Sinaloa Cartel money launderer	Sentenced to 96 months for laundering money on behalf of Chapo Guzman
IDENTITY THEFT	Rashia Wilson, Self-Proclaimed Queen of Tax Fraud	Serving 21 year prison term

Criminal – CI Field Offices



*The Las Vegas field office merged into the Phoenix field office in July 2020.

IRS Criminal Enforcement Efforts – CI Nationally Coordinated Investigations Unit (NCIU)



Formed 5/1/2017

Virtual currency/cryptocurrency is a current NCIU Priority

Strong partnerships within IRS and external stakeholders

Focuses on developing investigative strategy that addresses nationwide key noncompliance areas and emerging threats

Uses data driven case selection (with Research, Applied Analytics & Statistics (RAAS)) to find and investigate financial crimes

Nationally Coordinated Investigations Unit (NCIU)



- **Vision Statement:** To utilize a data driven approach to support field operations by enhancing existing case development projects and by identifying and referring impactful leads for further investigation.
- **Mission Statement:** To partner with: other operating divisions and external contacts to identify emerging or high-risk tax evasion and money laundering schemes, data analytics experts to build algorithms to detect individuals engaging in such schemes, internal and external data experts to obtain third-party data and access to technology which will lead to advances in the quality of referrals and will enable NCIU to tailor referral to meet the needs of our customers.

Initiatives

- Employment Tax
- International
- Tax Exempt Entities
- Abusive Schemes
- Virtual Currency
- 1099-K
- COVID-19 Related Fraud
- Social Media
- Schedule C
- Financial Institution Integrity and Third-Party Professional Money Laundering



Focus on International Tax Enforcement and Cryptocurrencies

IRS Enforcement Efforts – Sources of Information International



Traditional methods of case/issue identification in a domestic context generally do not work in the offshore

Turn to outside sources of information

- John Doe summons
- Whistleblower information
- Offshore Voluntary Disclosure Program
- Data mining of Swiss Bank Program and other information continues
- Exchange of Information
- FATCA Reporting
- Data analytics, open-source information and use of sophisticated AI methods
 - **CI Specific – MLATs, trash pulls, undercover, J5 (Joint Chiefs of Global Tax Enforcement), NCIU**

Civil International Tax Enforcement



- Oct. 2018 - WDTX authorized John Doe summons to **Taylor Lohmeyer** seeking “[a]ll books, papers, records, or other data in your possession, custody, or control concerning the provision of services to U.S. clients relating to the acquisition, establishment or maintenance of offshore entities or structures of entities.” TL moved to quash on the ground of identity privilege. Court granted petition to enforce the summons, but granted TL option to submit privilege log. TL declined and appealed.
 - 5th Circuit affirmed (957 F.3d 505). **On Oct. 4, 2020, SCOTUS denied cert.**
- Jul. 29, 2021 – SDNY authorized John Doe summons to **multiple couriers and financial institutions** to produce information about U.S. taxpayers who may have used the services of **Panama Offshore Legal Services (“POLS”)** and its associates to evade federal income taxes.
- IRS seeks to trace deliveries and EFTs between POLS and its clients, to identify POLS U.S. clients who used POLS to create or control foreign assets and entities to avoid U.S. tax compliance.
- Sept. 16, 2021 – District Court (Minnesota) authorized John Doe summons to **MoneyGram Payment Systems** related to investigation into U.S. taxpayers who used POLS. The IRS seeks information regarding U.S. taxpayers who, at any time during years 2013-20, used POLS to establish, maintain, operate, or control any foreign corporation, company, trust, foundation or other legal entity; or any foreign or domestic financial account or other asset in the name of such foreign entity.

IRS CI Units – International



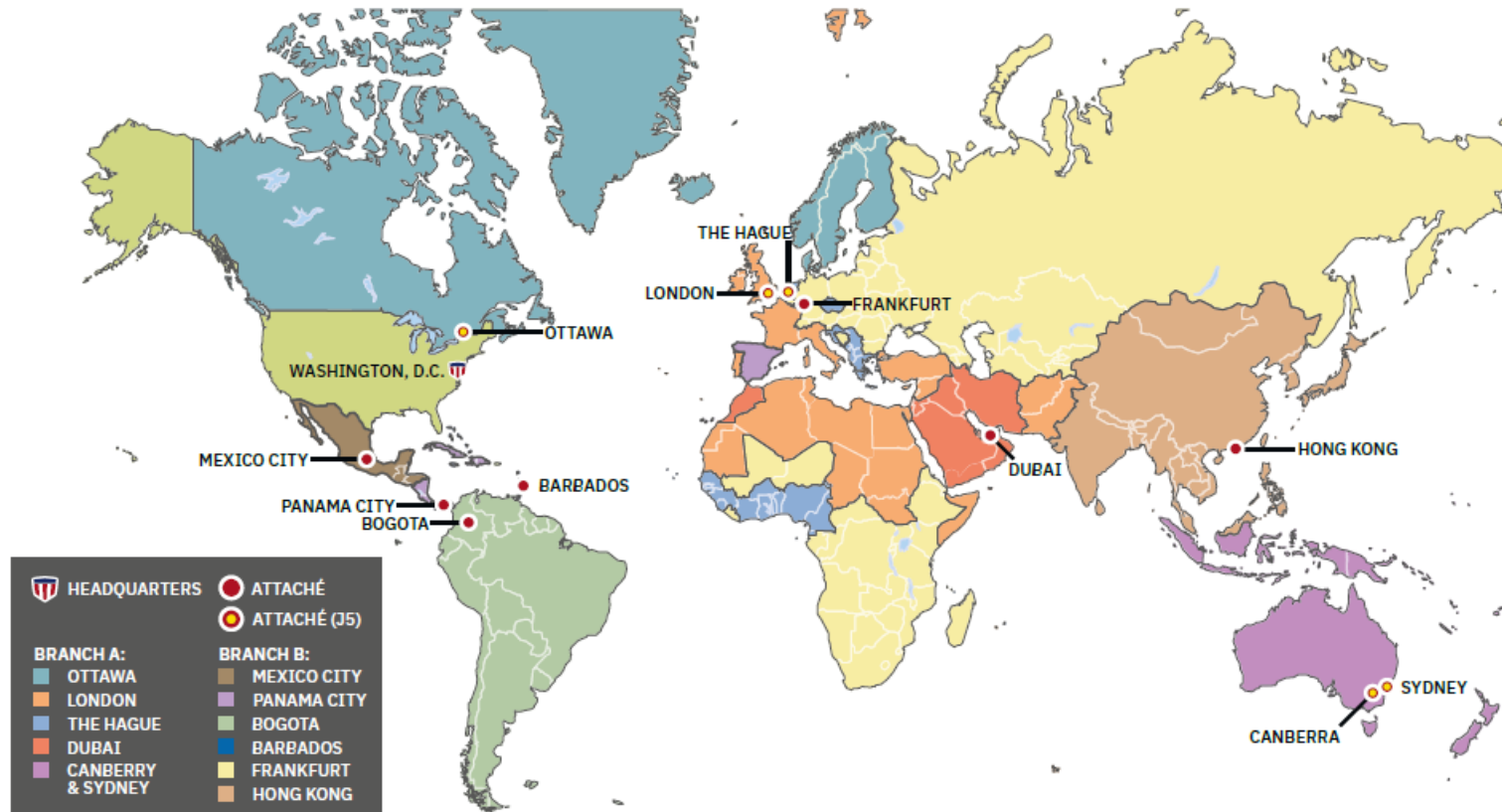
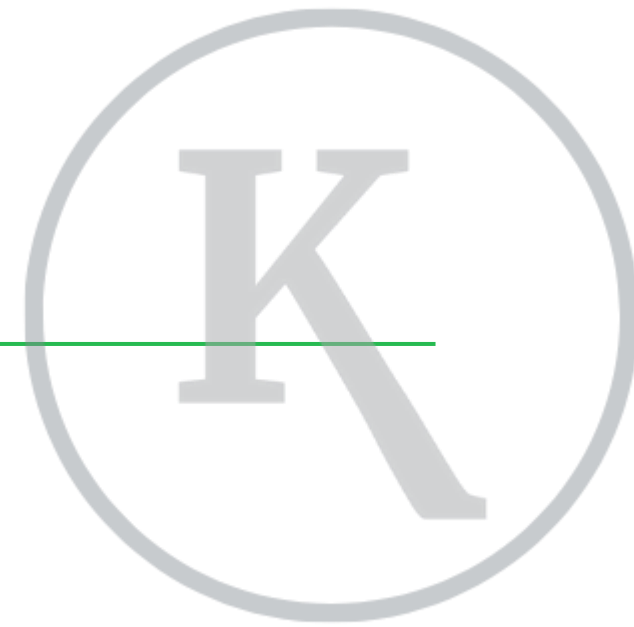
International Presence

- Only division with physical int'l presence
- Attachés located in 11 countries (Germany, China, England, Australia, the Netherlands, Colombia, Barbados, Mexico, Canada, UAE and Panama)
- Feb. 2018 – new international tax enforcement group of 10 Special Agents to focus on international crimes by tax evaders who use cryptocurrency
- FY19-22: 740 international pros recommendations. 12.1% of Special Agents investigative time is directed to international related investigations.

International Tax & Financial Crimes Initiatives

- **Ex-Patriates** - Investigation of U.S. expatriates residing in foreign jurisdictions to include renunciations and purchase of economic citizenship through the EB-5 program
- **Offshore Compliance Initiative** - U.S. domesticated taxpayers using foreign abusive trusts, companies, accounts, transactions and structures to achieve a tax evasion purpose
- **FATCA** - Entities / individuals specifically engaging in schemes to evade the reporting requirements imposed by FATCA legislation
- **International Fugitives**
- **Private/public international Partnership**
- **Cybercrimes Attaches - Addressing the rapid worldwide cryptocurrency adoption and cybercrimes**
- new international tax enforcement group of ten criminal investigators to focus on international crimes by tax evaders who use cryptocurrency (Feb. 2018)

International Operations



J5



JOINT CHIEFS OF GLOBAL TAX ENFORCEMENT

Members

- **Australian Taxation Office (AU)**
- **Canada Revenue Agency (CA)**
- **Fiscale Inlightingen-en Opsporingsdienst (FIOD) (NE)**
- **HM Revenue and Customs (UK)**
- **IRS Criminal Investigation (US)**

Formed after November 2017 OECD meeting in London
Inaugural meeting in June 2018 in Canada

Committed to combatting transnational tax crime through increased enforcement collaboration.

J5 works together to gather information, share intelligence, conduct operations and build the capacity of tax crime enforcement officials.

Working Groups: Professional Enablers (UK), Cyber/Virtual Currency (US), Platforms/Data (NL), Public Private Partnerships (UK) and Media and Communications (US)

J5 Recent Activity

- 12/5/2022 – J5 launches international probe into the use of sales suppression software, prompted by the arrest of five individuals in the United Kingdom who allegedly designed and sold electronic sales suppression systems internationally.
- 08/25/2022 – Former Senior Executive of a US Department of Defense contractor pled guilty to tax evasion for providing false information to his return preparer and concealing more than \$500,000 in income. Three additional former defense contractor executives were also charged through this investigation.
- 08/12/2022 – Operator of a boiler room scheme sentenced to 10 years in federal prison and ordered to pay over \$2 million in restitution. The subject had been charged with conspiracies to commit securities fraud, wire fraud, and money laundering in a scheme that defrauded 17 victims of more than \$2 million.
- 06/30/2022 – The Office of the Commissioner of Financial Institutions (OCIF) of Puerto Rico issued a Cease and Desist Order and suspended operations of Euro Pacific International Bank, which is related to J5 Operation Atlantis.
- 05/14/2022 – J5 partners participated in a “Challenge” focused on identifying cross-border illegal crypto activity involving decentralized exchangers and non-fungible tokens (NFTS). The “Challenge” identified more than 50 leads to potential crypto financial crimes, including a potential \$1 billion Ponzi scheme.
- 04/28/2022 - J5 released an Intelligence Bulletin relative to NFTs to warn banks, law enforcement personnel, and private citizens about the dangers in dealing with NFTs.

Criminal International Tax Enforcement



- Oct. 2020 – **Robert Brockman** indicted in NDCA for 39 counts of tax evasion, wire fraud, money laundering, and other offenses related to an alleged decades-long scheme to conceal approximately \$2 billion in income from the IRS and to defraud investors in a software company’s debt securities using complex offshore structures and accounts in Switzerland and Bermuda. **Brockman died in August 2022. The related prosecution in NDCA – *U.S. v. Carlos Kepke* – also ended with the death of Mr. Kepke on the eve of trial in November 2022.** Civil proceedings (forfeiture and jeopardy assessments) continue...
- Sep. 2021 – **Mark Gyetvay** indicted in MDL for wire fraud, failure to file FBARs, tax evasion, willfully filing false returns, assisting preparation of false returns, and willful failure to file returns in connection with efforts to conceal substantial offshore assets and foreign source income. **Trial set for March 2023.**
- Sep. 2021 – Indictment of 6 executives (Ivo Bechtiger, Bernhard Lampert, Peter Rüegg, Roderic Sage, Rolf Schnellmann and Daniel Wälchli) and **Zurich-based Allied Finance Trust AG** unsealed alleging defendants helped taxpayers hide income in accounts at Privatbank IHAG in Zurich and other locations using “Singapore Solution.”
 - **Wayne Franklyn Chinn** pled guilty to evasion for concealing roughly \$5 M in IHAG accounts funded from nominee accounts in Hong Kong and held in the name of a Singapore-based trust company acting on behalf of two sham foundations.

Digital Asset/Cryptocurrency Tax Enforcement

(Civil and Criminal Perspective)



John Doe Summons (JDS) Activity - Digital Assets



Nov. 30, 2016 – Court (N.D. Cal.) authorized IRS to serve a JDS on Coinbase, the largest U.S.-based virtual currency exchange

- Summons required production of information on accounts with at least the equivalent of \$20,000 in any one transaction type (buy, sell, send or receive) in any one year between 2013 and 2015, to include: (1) taxpayers' identification number; (2) name; (3) birth date; (4) address; (5) record of account activity; and (6) all periodic statements of account

Mar. 30, 2021 – JDS filed seeking information on U.S. taxpayers with accounts with two cryptocurrency exchanges and have conducted at least \$20,000 in transactions in any given year from 2016 through 2020

- Kraken (N.D. Cal.) – Court approved a narrowed scope JDS to Payward Ventures Inc. d/b/a Kraken; excluded customer correspondence and certain “know-your-customer” responses
- Circle (D. Mass.) – Court approved initial JDS on Circle Internet Financial Inc., or its predecessors, subsidiaries, divisions, and affiliates, including Poloniex LLC

Aug. 8, 2022 – JDS filed seeking information on U.S. taxpayers who have accounts with SFOX and have and have conducted at least \$20,000 in transactions in any given year from 2016 through 2021

- SFOX (C.D. Cal.) – Court authorized the IRS to serve a JDS on SFOX, a cryptocurrency prime dealer headquartered in Los Angeles, California, seeking information about U.S. taxpayers who conducted at least \$20,000 in transactions in cryptocurrency between 2016 and 2021 with or through SFOX
- M.Y. Safra (SDNY) – Court authorized the IRS to serve a JDS on bank M.Y. Safra; SFOX has partnered with M.Y. Safra to offer SFOX users access to cash-deposit bank accounts.

IRS Campaign Audits and Voluntary Disclosures



Jul. 2 2018 - IRS Announces Virtual Currency as a Campaign Audit

Virtual Currency

Practice Area: Withholding & International Individual Compliance

U.S. persons are subject to tax on worldwide income from all sources including transactions involving virtual currency. IRS Notice 2014-21 states that virtual currency is property for federal tax purposes and provides information on the U.S. federal tax implications of convertible virtual currency transactions. The Virtual Currency Compliance campaign will address noncompliance related to the use of virtual currency through multiple treatment streams including outreach and examinations. The compliance activities will follow the general tax principles applicable to all transactions in property, as outlined in Notice 2014-21. The IRS will continue to consider and solicit taxpayer and practitioner feedback in education efforts, future guidance, and development of Practice Units. Taxpayers with unreported virtual currency transactions are urged to correct their returns as soon as practical. The IRS is not contemplating a voluntary disclosure program specifically to address tax non-compliance involving virtual currency.

Note: In Aug 2018, FinCEN reports that 1,500 SARs every month involving virtual currency

Apr. 2019 - Form 14457, Part 1 (voluntary disclosure preclearance request) updated to include virtual currency

Virtual Currency: Educational Letters



- Jul. 2019: IRS sent “educational” letters (Letters 6173) to 10,000+ taxpayers who engaged in virtual currency transactions and possibly failed to report and pay tax on transactions. See IR-2019-132.
 - Letters were intended to “help taxpayers fully understand and meet their obligations”
 - Addresses taxpayers who the IRS (a) knows have or had one or more virtual currency accounts and (b) believes may have been required to file a tax return, form, or schedule reporting virtual currency transactions for the 2013 through 2017 tax years, but did not
 - Requests a response from the taxpayer, potentially including a declaration made under penalties of perjury, irrespective of whether the taxpayer believes that he or she properly reported all items
- The IRS followed these educational letters with Letters 6174 and 6174-A

IRS OFE - Operation Hidden Treasure



Mar. 5, 2021 - IRS announces Operation Hidden Treasure

- Partnership between OFE and CI to investigate taxpayers who do not report cryptocurrency transaction
 - Pairs revenue agents with third-party specialists
 - Third-party contractors to aggregate, value, and compute gains and losses
- Refer appropriate cases from OFE to CI
- Looking to:
 - Structuring
 - Use of nominees and/or shell entities
 - Moving between on-chain and off-chain transactions
 - Other indicia of fraud

Continued Cryptocurrency Enforcement



First six months of 2021 – 458 ransomware related transactions reported on SARs with a total value of \$590 M (42% increase from 2020) (cryptocurrency is primary method of payment)

Jan. 2022 - Form 1040 for the 2021 tax year includes the question “At any time during 2021, did you receive, sell, send, exchange, or otherwise dispose of any financial interest in any virtual currency?”

Feb. 15, 2022: Form 14457, **Voluntary Disclosure Practice Preclearance Request and Application** revised to include an expanded section on reporting virtual currency.

Feb. 17, 2022: DOJ named AUSA Eun Young Choi (prosecutor in the Panama Papers investigations), Director of National Cryptocurrency Enforcement Team (formed on Oct. 6, 2021, to tackle complex investigations and prosecutions of criminal misuses of cryptocurrency, particularly crimes committed by virtual currency exchanges, mixing and tumbling services, and money laundering infrastructure actors)

Nov. 11, 2022: **FTX** commences Chapter 11 bankruptcy proceedings.

IRS CI has prioritized training and deployment of cryptocurrency, blockchain and open-source intelligence (OS-INT) technologies to investigate complex cyber-financial criminal schemes

- Cyber Crimes Unit (DC and LA) and Advanced Collaboration & Data Center (ACDC) in northern VA

Continued Cryptocurrency Enforcement



Announcement 2023-2: Section 80603 of the Infrastructure and Investment and Jobs Act clarifies and expands the rules regarding the reporting of information on digital assets by brokers under IRC 6045 and 6045A.

- The announcement clarifies that until the IRS issues new final regulations under section 80603 with respect to IRC 6045, a broker may continue to report gross proceeds and basis as required under existing law and regulations.
- In addition, until the IRS issues new final regulations under section 80603 with respect to IRC 6045A, a broker may continue to issue statements on transfers of covered securities as required under existing law and regulations.
- Brokers will not be required to report additional information with respect to dispositions of digital assets, issue additional statements, or report to the IRS on transfers of digital assets until those new final regulations under IRC 6045 and 6045A are issued.

Reminder - Parallel Proceedings!



Defined: Multiple investigations or litigations arising from same facts or transactions; brought by combination of govt agencies – civil, criminal, or administrative; and in tandem or in succession, addressing different public interests

History:

Criminal and civil investigations *in seriatim*, with civil referrals to years later
Civil referrals were often only made when evidence insufficient for indictment
Parallel proceedings were authorized but not frequent

Justice Department Policies in Tax Matters - Justice Manual 6-4.400

Tax Division uses all available judicial remedies and procedures to enforce tax laws: prosecutions, civil injunctions, summons enforcement, collection actions, and defense of civil refund suits, simultaneously or sequentially.

Today - Substantial increase in parallel proceedings

Criminal investigations, civil audits and investigations, Congressional inquiries, etc.
Civil proceedings often result in civil fraud penalties – 75% of tax due

Practice Tips:

Scope of Prosecution Team

Consider discovery issues (and FOIA requests)

Brady v. Maryland, 373 U.S. 83 (1963)

- Due Process Protection Act, effective October 1, 2020
- F.R.Crim.P. 5(f), *Reminder of Prosecutorial Obligations*

Best Practices

- In addition to its current budget, IRS received supplemental 10-year funding totaling almost \$80B as part of the Inflation Reduction Act.
- Funding will be used to bolster technology, customer service, hiring and compliance efforts.
- IRS Divisions are working closer together and expect the fraud referral program to grow.
- Expect Cryptocurrency and International compliance efforts to continue
- IRS increasingly turns to data analytics as means of developing and refining cases (“beware of your digital footprint”)
- IRS is very interested in pursuing “professional enablers” in civil and criminal enforcement.
- Remember that today’s civil audit or civil collection matter could become tomorrow’s criminal investigation.





Thank you!
