Senator Chuck Grassley
Kathryn Keneally
Nominee, Assistant Attorney General (Tax), U.S. Department of Justice
Questions for the Record

1. In 2006, I authored changes to the longstanding whistleblower provisions at the IRS. The changes were made to incentivize whistleblowing on big-dollar tax fraud. A recent GAO report indicates that my efforts were successful. The IRS has received tips on more than 9,500 taxpayers from 1,400 whistleblowers in just five years. However, I remain concerned that the IRS, like the Justice Department with the False Claims Act revisions I authored in 1986, continues to treat whistleblowers like skunks at a picnic. For example, the IRS's offshore compliance programs likely would not have achieved the success it has without the information it received from a foreign bank employee. Yet, as I stated in a letter to the IRS Commissioner in June, 2010, I have serious doubts that the IRS effectively utilized the information provided to it by the UBS whistleblower. Information from whistleblowers should result in easy money for the IRS – which is really easy money for the federal government. In the UBS case, the Department of Justice sat on the information provided by the whistleblower for a very long time before acting on it. The IRS has a policy that whistleblower cases will not be prioritized over other audits.

    a. Do you agree with this policy?

Answer: The legislative changes enacted as part of the Tax Relief and Health Care Act of 2006 made important changes to the IRS whistleblower policy, most significantly by requiring the creation of an IRS Whistleblower Office and mandating payment to whistleblowers under the conditions set out in Section 7623(b) of the Internal Revenue Code. I believe that these provisions greatly strengthened the policy concerning whistleblowers, and created a valuable tool for tax enforcement. While I am not familiar with an IRS policy not to give whistleblower cases priority treatment, I believe that information provided to the IRS Whistleblower Office is very valuable to tax enforcement.

    b. What steps will you take to ensure the success of the IRS whistleblower program?

Answer: While I understand that the IRS whistleblower program functions as part of the IRS and not as part of the Department of Justice Tax Division, I believe that the whistleblower program is an important part of tax enforcement. If I am given the opportunity to serve as the Assistant Attorney General of the Tax Division, I will work diligently to further a strong working relationship between the Department of Justice Tax Division and the IRS, including the IRS Whistleblower Office.

    c. Attorney General Holder is aware of my concerns about whistleblower claims languishing at the Justice Department. Will you work with him to prioritize tax whistleblower cases?

Answer: If I am so fortunate as to be confirmed, I will communicate within the Department of Justice my respect for the IRS Whistleblower Office, and for the important role of whistleblower cases in tax enforcement.

2. On several occasions you have expressed opposition to the federal sentencing guidelines. In an article you wrote in the August 2004 edition of *White Collar Crime*, you used the sentence given to an executive of Dynergy Inc., who was indicted for accounting fraud, to argue that the sentencing guidelines have failed in their objective to create uniformity and proportionality in sentencing. You further argued that the "the current guideline system is not honest." Do you continue to have concerns about the sentencing guidelines? Please explain.

   Answer: I do not continue to have the concerns about the U.S. Sentencing Guidelines that I expressed in the August 2004 edition of *White Collar Crime.* I believe that judicial decisions since that time have remedied these concerns. I am in agreement with the original objective of the Guidelines to create uniformity and proportionality in sentencing. I began my practice before the enactment of the Guidelines, and had personal experience with the extreme variation in sentencing that occurred between similarly situated defendants prior to the Guidelines. I believe that the Guidelines as currently interpreted and applied strike a good balance between the pre-Guidelines failure of sentences to be uniform and proportionate, and the post-Guidelines anomalies discussed in my August 2004 article. I served for many years as a member of the Practitioners' Advisory Group to the U.S. Sentencing Commission. I have not been in general opposition to the Guidelines, but have instead worked for the improvement of the Guidelines.

3. As the Assistant Attorney General for the Tax Division will your views on the Guidelines inhibit you in any way from prosecuting suspected tax evaders to the full extent of the law?

   Answer: If I am confirmed, I will use and encourage the use of the tools available for effective tax enforcement, including the Guidelines. I hold no views, either with regard to the Guidelines or any other aspect of tax enforcement, that would inhibit me in any way from prosecuting suspected tax evaders to the full extent of the law.

4. You have been highly critical of DOJ Directive No. 128, which provides guidance for charging individuals with mail and wire fraud conspiracy in lieu of, or in addition to, criminal tax charges. As the Assistant Attorney General for the Tax Division will you seek to modify this directive? If so, how?

   Answer: I am in agreement with the general principles stated in Directive 128, and with the examples provided in Directive 128 concerning the types of circumstances that might warrant the authorization of charges in lieu of or in addition to tax charges. It is my view that, in the seven years since the issuance of Directive 128, the standards set out in Directive 128 have been applied with careful regard to the principles and goals of tax enforcement. I do not believe that the concerns that I expressed in the early period following the issuance of Directive 128 have been borne out by its implementation. In general, I do not believe in fixing something that does not appear to be broken. While there may be some extraneous language in

Directive 128 that could be stated more clearly, if I am confirmed as Assistant Attorney General for the Tax Division, I would not seek to change the core principles of Directive 128.

5. All federal agencies are facing budget cuts. As a result, these agencies, including the IRS and the Department of Justice, need to do a better job of allocating their resources to ensure the best bang for the buck. What are your recommendations for targeting these limited resources?

   Answer: It is of central importance that the Tax Division focus enforcement activity in a manner that fosters voluntary compliance with tax laws by all taxpayers. The Tax Division's Offshore Compliance Initiative is an excellent example of a program that has relied on civil and criminal tax enforcement to encourage large numbers of taxpayers to make voluntary disclosures of past wrongdoing. This initiative should be continued, and looked to as a model. It is also always important to pursue tax professionals who engage in tax evasion or abusive tax avoidance, for example through the promotion of fraudulent schemes, the preparation of false tax returns, or personal non-compliance. Civil and criminal enforcement against such tax professionals can have a broad impact in general and specific deterrence.

   The Tax Division must look to the IRS for case development and referrals. If I am confirmed, I will make every effort to foster a strong relationship between the Tax Division and the IRS, and to encourage the development of those cases that will have the greatest impact. In this regard, as previously stated, I will remain aware of the potential benefits of cases that can be developed through the IRS whistleblower program.

6. If confirmed, what will be your biggest challenges? How will you address those challenges?

   Answer: I believe that the previous question identified what will likely be the biggest challenge for the Tax Division: the effective allocation of increasingly limited resources for the greatest impact on tax compliance. If I am given the opportunity to serve as Assistant Attorney General for the Tax Division, I will work to prioritize those enforcement efforts, such as the Offshore Compliance Initiative, that will further this goal. If confirmed, I will also work to strengthen the good relationship between the Tax Division and the IRS, and to take the greatest advantage of IRS activities, such as its whisteblower program, to further tax enforcement.

7. What goals will you set for the first year on the job?

   Answer: If I am so fortunate as to be confirmed, my first goal will be to listen and to learn about the current enforcement efforts of the Tax Division. The Tax Division has currently identified the Offshore Compliance Initiative as its top litigation priority, and I agree with that position. I also believe that enforcement against tax professionals who promote fraudulent schemes, prepare false tax returns, or personally commit tax crimes, should be an enforcement priority, through criminal prosecution and civil enforcement, including injunction actions. I also recognize and, if confirmed, will be committed to enforcement against those who seek to undermine our tax system by wrongly denying the legitimacy of our tax laws .

8. Do you think that IRS Criminal Investigations should be permitted to work directly with US Attorneys instead of having DOJ Tax approval in most cases?

Answer: I strongly support the policy by which the Tax Division reviews and authorizes criminal tax charges. The tax system touches all U.S. citizens, residents, and those who earn income in this country. Ensuring that the tax laws are enforced fairly and consistently is central to the mission of the Tax Division. I have practiced in the Southern District of New York, where it is my understanding and has been my experience that there are many instances in which IRS Criminal Investigation works directly with the U.S. Attorney's Office in grand jury investigations of criminal tax cases. In jurisdictions, such as the Southern District of New York, that develop local prosecutorial tax expertise, this cooperative effort can be a valuable and efficient use of resources. I believe it remains important that the Tax Division retain the final authority to approve tax charges even in such circumstances.

9. How much time do you think is appropriate for IRS CI agents to spend on assisting Justice Department prosecutions that are not tax-related? What benefit does the Justice Department derive from using such assistance when such resources may be better used for tax enforcement? Aren't we robbing Peter to pay Paul by using resources for non-tax issues?

   Answer: The United States faces great challenges as a result of the tax gap, and IRS agents are on the front line of addressing this challenge. The first priority for IRS agents should be the fair and consistent enforcement of tax laws, to address the tax gap challenge and to ensure that those taxpayers who are in tax compliance can have confidence that there will be enforcement against those who are not in compliance. I believe, based on my experience, that IRS Criminal Investigation special agents are by training and experience among the very best in the world at investigating financial transactions and developing evidence of financial crime. There may be exceptional circumstances, such as anti-terrorism enforcement, when it may be appropriate that the skills of IRS agents be used to meet other national needs.

10. Do you believe that dual purpose summonses are appropriate?

    Answer: Yes. The Supreme Court determined in *Tiffany Fine Arts, Inc. v. United States*, 469 U.S. 310 (1985), that dual purpose summonses do not need to meet the requirements for John Doe summonses set out in Internal Revenue Code section 7609(f).

11. Due to the controversy surrounding the use of the term "tax protester", a recent Assistant AG for Tax coined the term "tax denier." Do you agree with this terminology and do you expect to use it?

    Answer: I agree wholeheartedly that enforcement against individuals who willfully refuse to accept the legitimacy of U.S. tax laws must be a priority. I also believe strongly that it is essential to use criminal and civil enforcement, including injunction actions, to stop those who promote schemes to encourage non-compliance with U.S. tax laws. I recognize the issues concerning the term "tax protester." In my view, the individuals who fall into the category defined as "tax deniers" or "tax defiers" are simply tax cheats. The terms "tax deniers" or "tax defiers" are fine terms. The important issue is that there be enforcement against such individuals, who are engaged in wrongful conduct, not free speech. I would like to note that while I have represented many individuals and companies in civil and criminal tax litigation, because "tax deniers" or "tax defiers" insist on making arguments that have no basis in law, I have never represented anyone who falls in this category.

12. What changes would you suggest to the civil injunction program to combat abuse by preparers?

    Answer: Enforcement against tax professionals who promote fraudulent schemes, prepare false tax returns, or personally commit tax crimes, should be an enforcement priority, through criminal prosecution and civil enforcement, including injunction actions. The past decade has seen a significant increase in the Tax Division's use of civil injunctions against tax fraud promoters and fraudulent return preparers. I understand that the Tax Division participates in IRS training classes and conferences to help IRS agents and attorneys learn how to conduct an investigation that leads to a successful injunction referral. Fostering this strong working relationship between the Tax Division and the IRS will benefit the civil injunction program and other areas of tax enforcement.

13. Do you believe the current number of such injunctions has a sufficient deterrent effect?

    Answer: Civil injunctions have a strong deterrent effect, by shutting down the activities of tax fraud promoters and fraudulent return preparers, and also by sending a message that deters others from ever engaging in such activity. It is my understanding that the Tax Division is strongly committed to this enforcement tool, and I support that commitment. Because I am not at the Tax Division, I cannot say whether the current number of injunctions is sufficient, or whether more resources can and should be directed at this effort.

14. What role should the DOJ Tax Division have in distinguishing aggressive tax planning from obstruction of justice, i.e., KPMG and UBS?

    Answer: The fair and consistent enforcement of the tax laws is a central part of the stated mission of the Tax Division. To meet this mission, the Tax Division must determine whether tax violations should be pursued through criminal or civil enforcement, or a combination of both. When aggressive tax planning results in the underpayment of tax, there should be civil enforcement to recover tax, interest, and appropriate penalties. When aggressive tax planning crosses the line into fraudulent activity, criminal prosecution may be appropriate, depending on the evidence and available prosecutorial resources. In either circumstance, the use of civil injunctions can be an effective general and specific deterrent. Obstruction of justice is a crime, and should be prosecuted as such.

15. How would you coordinate the activities of the Southern District of New York and other U.S. Attorneys' offices that are outside the direct supervision of the AAG for Tax? Do you think the tax function of the Southern District of New York should be placed under the supervision of the AAG for Tax?

    Answer: If I am given the opportunity to serve as the Assistant Attorney General for the Tax Division, I would commit myself to fostering strong working relationships with local U.S. Attorney Offices. I have practiced in the Southern District of New York, and it has been my experience and observation that the U.S. Attorney's Office has a respectful and cooperative relationship with the Tax Division in civil and criminal tax matters. In jurisdictions, such as the Southern District of New York, that develop local prosecutorial tax expertise, this cooperative effort can be a valuable and efficient use of resources. In these jurisdictions, the Tax Division currently retains the final authority to approve criminal tax charges, and I believe that it is important that the Tax Division continue to exercise this authority.

16. What is your view of the Cheek defense? Do you believe that willful ignorance should ever be a defense to a criminal charge?

    Answer: The principal criminal tax statutes include a requirement that it be shown that the defendant acted willfully, which the Supreme Court reiterated in *Cheek v. United States*, 498 U.S. 198 (1990), "requires the Government to prove that the law imposed a duty on the defendant, that the defendant knew of this duty, and that he voluntarily and intentionally violated that duty." I believe that it is important that criminal sanctions be imposed for criminal conduct. However, given the complexity of the tax laws, criminal sanctions should not be imposed as a result of a good faith mistake or ignorance with regard to the tax laws. For this reason, I agree with the inclusion of the willfulness element in the criminal tax laws, and the definition of willfulness in *Cheek*. Subsequent to *Cheek*, several Circuit Courts have held that *Cheek* does not preclude that the jury be instructed that a defendant cannot make himself "willfully blind" (or in other words, "willfully ignorant") to the requirements of the tax laws. Further, the Supreme Court in *Cheek* also held that willfulness did not permit a defendant who objectively understood the tax law to assert his disagreement with the tax law as a defense.

17. Please describe with particularity the process by which these questions were answered.

    Answer: I reviewed each question. When appropriate, I reviewed publicly available materials relating to the questions. As examples, I reviewed the legislation and the IRS statements concerning its whistleblower program, information available on the Tax Division's website, and case law discussed in these answers. I prepared a complete first draft of answers to these questions. I received and considered comments from representatives of the Department of Justice. I prepared my final answers and forwarded them to the Department. I understand that the Department will submit my answers to the Committee.

18. Do these answers reflect your true and personal views?

    Answer: Yes.