



*Fraud and Abuse Are Addressed in the
Indian Tribal Sector, but Performance
Objectives and Measures Are Needed
to Assess Program Effectiveness*

January 28, 2013

Reference Number: 2013-10-018

This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.

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HIGHLIGHTS

FRAUD AND ABUSE ARE ADDRESSED IN THE INDIAN TRIBAL SECTOR, BUT PERFORMANCE OBJECTIVES AND MEASURES ARE NEEDED TO ASSESS PROGRAM EFFECTIVENESS

Highlights

Final Report issued on January 28, 2013

Highlights of Reference Number: 2013-10-018 to the Internal Revenue Service Acting Commissioner for the Tax Exempt and Government Entities Division.

IMPACT ON TAXPAYERS

The Indian Tribal Governments (ITG) office established the Abuse Detection and Prevention Team (ADAPT) to address potential fraud and abuse in the Indian tribal sector; however, specific performance objectives and measures are needed. Without performance objectives and measures, ITG office management cannot objectively determine that taxpayer funds expended on the ADAPT provide a good return on investment.

WHY TIGTA DID THE AUDIT

This review was initiated as part of TIGTA's Fiscal Year 2012 Annual Audit Plan and addresses the major management challenge of Tax Compliance Initiatives. The overall objective of this review was to determine whether the ITG office is taking action and measuring its accomplishments to stem the growth of fraud and abuse in the Indian tribal sector.

WHAT TIGTA FOUND

Although the ITG office established the ADAPT in Fiscal Year 2004 with the broad goal of stemming the growth of fraud and abuse in the Indian tribal sector, it has not developed specific performance objectives and measures. As a result, TIGTA could not determine if the ADAPT is effectively combating fraud and abuse in the Indian tribal sector. Setting specific measurable performance objectives would allow ADAPT management and staff to identify

strategies for what they want to achieve in the short and long term and provide assurance that taxpayer funds expended on the ADAPT provide a good return on investment.

While specific objectives and measures have not been developed, TIGTA found evidence that the ADAPT is actively identifying and addressing allegations of potential fraud and abuse by tribes and tribal members to meet its broad goal. Since Fiscal Year 2008, ADAPT examiners have investigated and referred eight potential fraud cases involving 10 entities to the National Fraud Office for further investigation (of which four were later referred to and accepted by Criminal Investigation). Also, ADAPT examiners have assessed tax, interest, penalty, and restitution amounts against Indian tribal entities and individuals totaling more than \$205 million (of which approximately \$75 million has been collected).

In addition, the ITG office has made several improvements to the ADAPT since our last report regarding the Tax Exempt and Government Entities Division's fraud program. For example, ITG office management improved the ADAPT by: 1) encouraging referrals of potential fraud and abuse, 2) formalizing examination approval procedures, 3) providing forensic accounting and fraud training to all ADAPT examiners, 4) increasing coordination with other stakeholders, and 5) assigning an experienced fraud coordinator to monitor and assist in the development of cases.

WHAT TIGTA RECOMMENDED

TIGTA recommended that the Director, ITG, develop specific performance objectives and measures in order to better assess ADAPT performance. In their response to the report, IRS management agreed with the recommendation and plans to review performance objectives and associated measures in other IRS fraud-related programs to determine whether, and at what level, similar standards can be implemented by the ADAPT. To the degree appropriate, the IRS plans to implement such standards.



TREASURY INSPECTOR GENERAL
FOR TAX ADMINISTRATION

DEPARTMENT OF THE TREASURY
WASHINGTON, D.C. 20220

January 28, 2013

MEMORANDUM FOR ACTING COMMISSIONER, TAX EXEMPT AND GOVERNMENT
ENTITIES DIVISION

Nancy A. Nakamura

FROM: (for) Michael E. McKenney
Acting Deputy Inspector General for Audit

SUBJECT: Final Audit Report – Fraud and Abuse Are Addressed in the Indian
Tribal Sector, but Performance Objectives and Measures Are Needed to
Assess Program Effectiveness (Audit # 201210018)

This report presents the results of our review on whether the Indian Tribal Governments office is taking action and measuring its accomplishments to stem the growth of fraud and abuse in the Indian tribal sector. This review was included in our Fiscal Year 2012 Annual Audit Plan and addresses the major management challenge of Tax Compliance Initiatives.

Management's complete response to the draft report is included as Appendix IV.

Copies of this report are also being sent to the IRS managers affected by the report recommendations. If you have any questions, please contact me or Gregory D. Kutz, Assistant Inspector General for Audit (Management Services and Exempt Organizations).



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Abbreviations

ADAPT	Abuse Detection and Prevention Team
FY	Fiscal Year
IRS	Internal Revenue Service
ITG	Indian Tribal Governments



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Background

Executive Order 13175¹ requires Federal agencies to maintain a government-to-government relationship with tribes, respect Indian tribal self-government and sovereignty,² honor tribal treaty and other rights, and strive to meet the responsibilities that arise from the unique legal relationship between the Federal Government and Indian tribal governments. Within the Internal Revenue Service (IRS), the Indian Tribal Governments (ITG) office³ is responsible for all Federal tax issues⁴ related to the 566 Federally recognized Indian tribes. The ITG office's mission is to help Indian tribes understand and comply with applicable tax laws and to protect the public interest by applying the tax law with integrity and fairness to all. According to the IRS, the ITG office accomplishes its mission through a balanced approach of outreach, education, compliance checks,⁵ and examinations conducted to determine Federal tax liabilities and filing requirements.

To carry out its responsibilities, the ITG office has established seven field groups. Five of these groups provide primary front-line service and are aligned to respect tribal affiliations wherever possible. These field groups consist of tribal government specialists who work in locations near the seats of tribal governments and address issues and provide guidance unique to the Indian tribal sector, *e.g.*, issues relating to tribal governments as employers, per capita distributions⁶ to tribal members, and the establishment of governmental programs, trusts, and businesses. The ITG office also established two field groups, collectively known as the Abuse Detection and Prevention Team (ADAPT) to address abuses and schemes that cause financial risk to the tribes and their tribal members.

According to ITG office management, effective interactions with sovereign tribal nations require knowledge of Federal Indian law and an awareness of unique tribal histories as well as an awareness that some tribes hold the view that they are not subject to *any* Federal tax law. This

¹ Executive Order 13175 was signed on November 6, 2000.

² Sovereignty refers to the right of Federally recognized Indian tribes to govern themselves.

³ The ITG office is a part of the IRS's Tax Exempt and Government Entities Division.

⁴ Generally, Federally recognized Indian tribal governments are not subject to Federal income tax. However, tribal-related entities are responsible for various income, employment, and excise taxes, as well as anti-money laundering and information reporting requirements. In addition, tribal members are subject to income tax.

⁵ Compliance checks are an important part of the ITG office's strategy to reduce the need for enforcement by keeping abreast of trends that are emerging among the tax filing and payment characteristics of tribal entities. Unlike an examination or audit, a compliance check does not seek to determine a tax liability for any particular period; it is voluntary, and the tribe may refuse to participate in a compliance check without penalty.

⁶ According to ITG office management, per capita distributions are payments made to all members of a tribe or to groups of members and can be from a variety of sources, including tribal trust assets or net revenues of gaming activity.



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view, combined with the growth in tribal economies,⁷ increases the risk that unscrupulous individuals can gain a foothold for illegal or unethical activities, including tax schemes, in the Indian tribal sector.

The ITG office established the ADAPT in Fiscal Year (FY)⁸ 2004⁹ to work issues where tax schemes or abuses¹⁰ affect multiple ITG office field group areas or involve extensive interactions with enforcement functions inside or outside the IRS. The ADAPT is comprised of ITG office specialists (hereafter referred to as examiners) experienced in the detection of fraud and abuse. ADAPT examiners generally do not have access to information for proactively identifying indications of the existence of fraud and abuse. Therefore, ADAPT examiners rely on referrals from individuals, other law enforcement officials, news articles, and other sources, including examinations of the books and records of Indian tribal entities, to detect indications of the existence of fraud and abuse.

Tax schemes may occur without the direct knowledge of a tribe, without an understanding of the consequences by a tribe, or with full involvement of a tribe. Many schemes result in income for Indian tribal members who may not be aware the schemes are illegal or unethical. The following are examples of schemes to avoid payment of tax:

- An Indian tribe may agree to claim ownership of a nontribal individual's business for a fee. The nontribal individual retains the profit and uses the nontaxable status of the tribe to avoid paying income taxes.
- An Indian tribal leader hires a company to provide services to the tribe and the tribe pays an inflated price to the company for services performed. However, part of the payment is then remitted back to a tribal leader, who does not claim it as income on his or her personal tax return, thereby diverting Indian tribal funds for personal use and avoiding income tax.
- An Indian tribe makes taxable per capita distributions of tribal funds to tribal members but does not report the distribution to the IRS in accordance with IRS reporting requirements. As a result, tribal members receiving the distribution may not report the

⁷ The rapid growth of the Indian gaming industry makes it the largest revenue producing gaming segment in the United States economy.

⁸ A 12-consecutive-month period ending on the last day of any month, except December. The Federal Government's fiscal year begins on October 1 and ends on September 30.

⁹ In FY 2004, the ADAPT consisted of one group. A second group of examiners was added in June 2009 to handle the increased volume of fraud and abuse referrals and to work civil fraud cases after the completion of criminal issues. To prevent bias, civil and criminal issues cannot be worked by the same examiners.

¹⁰ Although some of the work involves tax fraud, the team's role is much more expansive than that single issue, as it also encompasses tax shelter activities, Title 31 abuses, and the use of tribal entities to avoid proper reporting and oversight of transactions. In that regard, the team not only undertakes compliance actions to remedy identified noncompliance, but it is also charged with undertaking preventative actions to mitigate any growth in schemes.



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distribution on their personal income tax return, thereby not complying with tax laws and not paying tax on the distributed funds.

The ITG office's fraud efforts are conducted in conjunction with the National Fraud Program, which is established within the Small Business/Self-Employed Division. If indications of criminal fraud are identified by ITG office employees, the National Fraud Office provides guidance and refers cases to IRS Criminal Investigation for potential criminal prosecution.

This review was performed at the Tax Exempt and Government Entities Division ITG offices in San Bernardino, California; Albuquerque, New Mexico; Oklahoma City, Oklahoma; and Portland, Oregon, during the period November 2011 through September 2012. We conducted this performance audit in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective. Detailed information on our audit objective, scope, and methodology is presented in Appendix I. Major contributors to the report are listed in Appendix II.



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Results of Review

ITG office management established the ADAPT with the broad goal of stemming the growth of fraud and abuse in the Indian tribal sector; however, it has not developed specific performance objectives and measures. As a result, we could not determine if the ADAPT is effectively combating fraud and abuse in the Indian tribal sector. While specific objectives and measures have not been developed, the ADAPT is actively identifying and addressing potential fraud and abuse to meet its broad goal. In addition, the ITG office has made several improvements to the ADAPT since our FY 2003 report regarding the Tax Exempt and Government Entities Division's fraud program.¹¹

Performance Objectives and Measures Were Not Defined

The Government Performance and Results Act of 1993¹² requires agencies to set program goals and measure program performance against those goals. The guidelines are intended to increase agency accountability and improve the quality and delivery of Government services through goal setting, customer satisfaction, and results measurement.

ADAPT management established a broad goal but also stated that establishing specific performance objectives and measures is challenging. For example, ITG office management stated they were concerned about setting specific goals because the IRS Restructuring and Reform Act of 1998¹³ prohibits Records of Tax Enforcement Results (number of cases closed, dollars assessed, *etc.*) from being used to set performance goals or to evaluate individual ADAPT examiners.¹⁴ In addition, ITG office management stated that the size or population of fraud and abuse in the Indian tribal sector is unknown, making it difficult to set objective goals or measure how well the ITG office is addressing fraud and abuse overall. In addition, the ITG office cannot solely control the process of identifying and addressing fraud and abuse issues because it depends, in part, on the efforts of other agencies or offices.¹⁵

¹¹ Treasury Inspector General for Tax Administration, Ref. No. 2003-10-217, *The Tax Exempt and Government Entities Division Should Pursue Additional Methods to Identify Potential Fraudulent Activities* (Sept. 2003).

¹² Pub. L. No. 103-62, 107 Stat. 285 (codified as amended in scattered sections of 5 U.S.C., 31 U.S.C., and 39 U.S.C.).

¹³ Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

¹⁴ Enforcement results and program statistics can be reported at the national level.

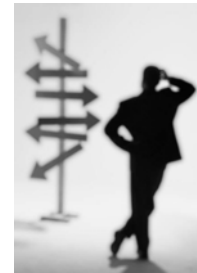
¹⁵ In addition, when addressing fraud and abuse issues, the work of examiners can be extensive and very unpredictable. The examiner's work must ensure a level of detail and documentation to withstand review by IRS Criminal Investigation, IRS Chief Counsel, Department of Justice staff, and the court system. This is especially difficult with tribal entities and individuals who may believe they are exempt from the Federal tax system.



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Although establishing performance objectives and measures can be difficult for a fraud program, establishing specific performance objectives would provide a better understanding of what the ADAPT is striving to accomplish and would provide a means for establishing methods to measure progress toward meeting short-term and long-term performance objectives. In addition, we determined that there is a knowledge base the ADAPT can draw upon. Based on our research, other IRS fraud-related programs, including IRS Criminal Investigation and the Small Business/Self-Employed Division National Fraud Program, have established objectives and measures regarding enforcement, customer satisfaction, examination timeliness, increased fraud and abuse outreach activities, the level of support and guidance provided to address issues, and support provided to other offices for case development. Setting similar performance objectives and developing methods of evaluating program success will provide valuable information for determining resources that should be applied to the ADAPT to prevent revenue loss to the Federal Government through fraud and abusive tax schemes. It may also provide increased enforcement and restitution assessments and assurance that taxpayer funds expended on the ADAPT provide a good return on investment.

Developing goals and measures would allow ADAPT management and staff to focus on what they would like to achieve in the short and long term.



Recommendation

Recommendation 1: The Director, ITG, should develop specific performance objectives for the ADAPT, along with associated measures, to better assess how effectively the program is addressing fraud and abuse in the Indian tribal sector.

Management's Response: IRS management agreed with this recommendation. The ITG office will review the performance objectives and associated measures in other IRS fraud-related programs to determine whether, and at what level, similar standards can be implemented by the ADAPT. To the degree appropriate, the ITG office will then implement such standards.

Indian Tribal Sector Fraud and Abuse Are Being Identified and Addressed

The ITG office has had significant fraud and abuse accomplishments compared to when we first reviewed fraud efforts in FY 2003. At that time, the ITG office generally had not developed a



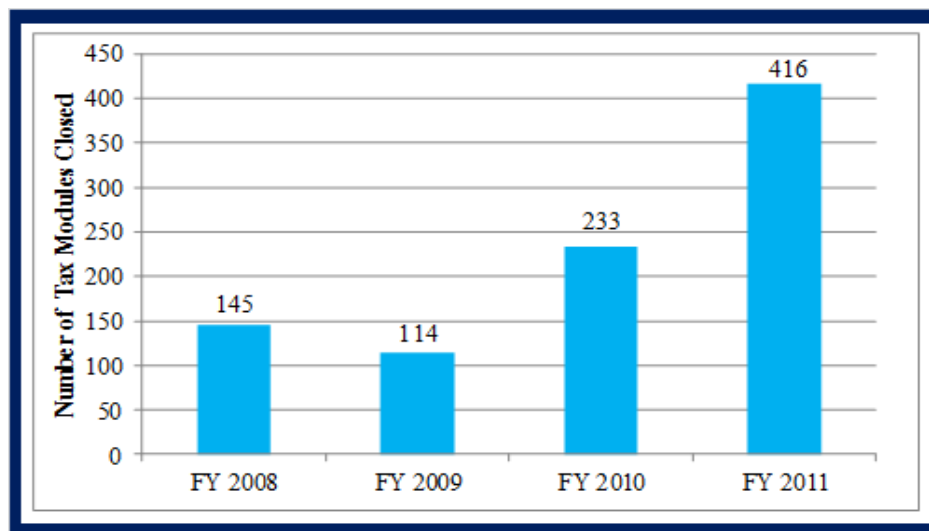
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program to combat fraud and abuse; rather, it focused its resources on assisting customers to correct noncompliance through customer education and outreach programs.

Since FY 2003, ITG office management has developed a fraud and abuse program through establishment of the ADAPT. Although ADAPT results are not tracked¹⁶ for the purpose of performance measurement, we identified evidence of the following achievements since FY 2008.

- **The ADAPT is actively examining allegations of Indian tribes and tribal members potentially involved in fraudulent or abusive activities.** From FY 2008 through FY 2011, the ADAPT completed examinations of 95 Indian tribal entities and 203 tribal members (related to 68 (12 percent) of 566 Federally recognized Indian tribes) due to indications of potential fraud or abuse.¹⁷ Due to the fraud and abuse identified in the tribal sector, a second group of examiners was added to the ADAPT in June 2009. Figure 1 shows the significant increase in the number of examinations of tax modules¹⁸ closed after addition of the second group.

Figure 1: Number of Tax Module Examinations Closed From FY 2008 Through FY 2011



Source: Treasury Inspector General for Tax Administration analysis of ITG office records for FY 2008 through FY 2011.

¹⁶ The ITG office does not track the results of cases because it does not have a computer system to track enforcement actions the ITG office takes or subsequent enforcement actions taken by other functions of the IRS.

¹⁷ The ITG office normally performs only examinations of Indian tribal entities. However, several large schemes were identified involving the transfer of tribal funds to individual tribal members representing taxable income to the individual, but no payment of tax was made. ADAPT examiners worked these cases because other ITG office examiners were not trained to perform examinations of Forms 1040, *U.S. Individual Income Tax Return*.

¹⁸ Tax modules are defined as one tax period for one tax return. For example, an individual Form 1040 for Tax Year 2010 is one tax module, while the same form for Tax Year 2009 is a second module.



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At the close of our audit, the ADAPT had open examinations on 42 individual and tribal entities (141 tax modules) related to potential fraud and abuse schemes. In addition, other cases were awaiting assignment to ADAPT examiners for examination or suspended pending settlement of criminal charges, grand jury action, or the results of examiners working with Criminal Investigation on other cases.

- **The ADAPT has assessed a significant amount of taxes, penalties, and interest as a result of examinations.** From discussions with ADAPT management and through analysis, we determined that since FY 2008, tax, interest, penalty, and restitution assessments were made against Indian tribal entities and individuals totaling more than \$205 million.¹⁹ Of this amount, the IRS has collected approximately \$75 million. The remaining \$130 million is either in Appeals²⁰ or awaiting adjudication through the courts. For example, in April 2012, a former tribal council leader pled guilty and agreed to pay more than \$5 million for distributing tribal funds to himself and family members without reporting it as income for tax purposes.

In April 2012, a former Indian tribal council leader pled guilty and agreed to pay more than \$5 million for distributing tribal funds to himself and family members without reporting it as income for tax purposes.



- **The ADAPT referred potential fraudulent activities to Criminal Investigation for potential prosecution.** Between FYs 2004 and 2007,²¹ the ITG office referred 10 cases (involving 28 entities) that were accepted by the National Fraud Office for further development. Four of the 10 cases (19 entities) were later accepted by Criminal Investigation for further investigation. From October 2007 through January 2012, the ITG office referred eight cases (involving 10 entities) to the National Fraud Office for further development. Four of the eight cases (involving four entities) were referred to and accepted by Criminal Investigation for further investigation. For the remaining four cases, the National Fraud Office took no action on two cases, asserted a civil penalty on one case, and Criminal Investigation declined one case.

¹⁹ This figure could be more than stated. We did not review all assessments for the period because that information was not available in management reports. Instead, we identified and discussed individual cases involving assessments, penalties, and interest totaling more than \$5 million with ADAPT management.

²⁰ The IRS Appeals office is separate from and independent of the office that completes examinations and recommends adjustments to tax returns. IRS customers can file with the Appeals office to review proposed examination adjustments.

²¹ Treasury Inspector General for Tax Administration, Ref. No. 2009-10-096, *A Corporate Approach Is Needed to Provide for a More Effective Tax-Exempt Fraud Program* (Jul. 2009).



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Program Changes Have Enhanced the Indian Tribal Governments Office's Ability to Identify and Address Fraud and Abuse

We reviewed actions taken by ITG office management since FY 2008 and determined that a number of changes have been made to improve the ability to identify and address Indian tribal tax fraud. For example, ITG office management improved the ADAPT by: 1) encouraging referrals of potential fraud and abuse, 2) formalizing examination approval procedures, 3) providing forensic accounting and fraud training to all ADAPT examiners, 4) increasing coordination with other stakeholders, and 5) assigning an experienced fraud coordinator to monitor and assist in the development of cases.

Presentations were given to encourage referrals of potential fraud and abuse

In a prior audit,²² we determined that the ADAPT made eight outreach presentations (averaged four per year) during FY 2006 and FY 2007 at Indian gaming conferences. Since October 2007, the ADAPT has made 24 outreach presentations (averaged six per year) in an effort to deter fraud and abuse by creating a greater awareness of tax code violations, improving gaming cooperation in investigations of financial crimes, and encouraging referrals when warranted.²³ These presentations are made at Indian gaming meetings such as the National Indian Gaming Association and to Federal agencies including the National Indian Gaming Commission and the Departments of Justice, the Interior, and the Treasury.

Examination approval procedures were formalized

Case building procedures were in place in the ADAPT prior to FY 2007 to provide assurance that only cases meeting ADAPT criteria were selected for examination and to provide enough information for ADAPT examiners to begin the examination efficiently. However, in FY 2009, a process was formalized requiring approval of all referrals²⁴ by the Director, Field Operations, or the Director, ITG, prior to assignment to an ADAPT examiner. This enhancement provides increased assurance that the specialized skills of ADAPT examiners are not used to conduct general examinations when higher profile fraud and abuse cases more suited to their skills are available. For our audit period, we determined that all cases in ADAPT examination inventory met ADAPT examination criteria.

²² Treasury Inspector General for Tax Administration, Ref. No. 2009-10-096, *A Corporate Approach Is Needed to Provide for a More Effective Tax-Exempt Fraud Program* (Jul. 2009).

²³ Referrals can originate from the examination of a third party where there is a financial interaction with a tribe or from other groups in the ITG office, the National Fraud Program, Criminal Investigation, the Federal Bureau of Investigation, the Department of the Interior, tribes and tribal members, or State departments of gaming. Referrals can be received through telephone calls, e-mails, paper documents, or the IRS Internet website.

²⁴ Managerial approval is not required if an open examination is expanded to include additional related entities or tax types and tax periods.



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ADAPT examiners were trained to increase skills in identifying and addressing fraud and abuse

Prior to FY 2008, ITG office management sent several ADAPT examiners to formal fraud training, including forensic accounting and expert witness courses. Since then, ADAPT management developed their own forensic fraud training material tailored to Indian tribal issues and provided training to all ADAPT staff in March and September 2009. In June 2011, additional training on the indicators of fraud, preparing criminal referrals, developing and asserting the civil fraud penalty,²⁵ joint investigations with other agencies, and other topics were provided to ADAPT examiners.

In addition, ADAPT management includes information on known schemes during training for ITG office and ADAPT examiners. Training helps ADAPT examiners sharpen their skills so they can effectively identify and address fraud and abuse in the Indian tribal sector.

The ITG office developed and provided training to all of its ADAPT examiners to increase skills for identifying and addressing Indian tribal fraud and abuse.



Stakeholders were provided information on the ADAPT to improve communications and working relationships

To enhance compliance, the ADAPT must work well with the National Fraud Program and Criminal Investigation. It is important that these stakeholders understand the types of fraud and abuse that can occur and be made aware of information on new schemes as they appear in the Indian tribal sector. Since FY 2008, ITG office management provided the following presentations:

- In September 2010 and July 2011, the ADAPT Fraud Coordinator developed and presented training classes to National Fraud Program officials to help them better understand fraud and abuse issues that occur within the Indian tribal sector.
- In August 2011, the ADAPT Fraud Coordinator developed and made a presentation to a Criminal Investigation Gaming Symposium. The presentation included information on the ITG office and the ADAPT, the ITG office customer base, fraud and abuse issues that occur within the Indian tribal sector, and ITG office fraud development procedures.

²⁵ Civil fraud results in a remedial action taken by the Government such as assessing the correct tax and imposing civil penalties as an addition to tax. Civil penalties are assessed as a part of the tax. Criminal fraud results in a punitive action with penalties consisting of fines and/or imprisonment. Criminal penalties are enforced only by prosecution, are provided to punish the taxpayer for wrongdoings, and serve as a deterrent to other taxpayers.



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- In November 2011, ADAPT management met with Criminal Investigation representatives to identify ways to improve communication regarding fraud and abuse within the Indian tribal sector. This resulted in the preparation of a “Frequently Asked Questions” document involving Indian tribes for use by Criminal Investigation special agents.

ADAPT monitoring reports are prepared more frequently, and an experienced coordinator was assigned to assist examiners and coordinate with stakeholders

ADAPT management used ad hoc status reports prior to FY 2008 to capture information on ADAPT open examinations with sensitive issues, examinations receiving media attention or involving litigation, and cases being worked with the National Fraud Program or sent to Criminal Investigation for potential prosecution. These reports help ITG office management monitor fraud and abuse examinations at various stages and identify those needing special attention. However, the reports are now prepared on a bimonthly basis to ensure the Tax Exempt and Government Entities Division Commissioner and others are aware of important issues affecting the ITG office, including issues that may receive media attention.

In addition, in August 2010 a new ITG office Fraud Coordinator was assigned with more than 15 years of experience in the IRS’s Special Enforcement Program²⁶ working fraud and abuse cases. The new coordinator provides experience working with IRS Criminal Investigation and IRS Chief Counsel to improve casework in preparation for potential litigation. In addition, the coordinator serves as a central point of contact for all ADAPT cases involving potential civil or criminal matters; assists ADAPT examiners on examinations with indications of fraud; monitors cases referred to the National Fraud Program for potential civil or criminal action; participates in monthly conference calls with other Tax Exempt and Government Entities Division fraud coordinators and representatives from the Small Business/Self-Employed Division National Fraud Program; and attends quarterly meetings with IRS Chief Counsel, National Fraud Program, and Criminal Investigation representatives. Having an experienced fraud coordinator who meets with other IRS stakeholders helps provide assurance that Indian tribal fraud and abuse issues are raised to other IRS stakeholders and the ADAPT is aware of fraud and abuse trends identified in other parts of the IRS.

²⁶ The Special Enforcement Program is a compliance program within the Small Business/Self-Employed Division directed toward the segment of the population that derives substantial income from either legal or illegal activities and intentionally understates their tax liability.



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Appendix I

Detailed Objective, Scope, and Methodology

Our overall objective was to determine whether the ITG office is taking action and measuring its accomplishments to stem the growth of fraud and abuse in the Indian tribal sector. To accomplish this objective, we:

- I. Determined whether ITG office management established performance objectives and measured the impact of ADAPT results on program goals.
 - A. Determined whether program goals had been clearly defined and documented according to the Government Performance and Results Act of 1993¹ and other performance standards.
 - B. Identified the process to assess the impact of the use of ADAPT staff since FY² 2008 to stem the growth of fraudulent and abusive activities in the Indian tribal sector.
 - C. Determined whether ADAPT management developed a process to track the number of cases that resulted in civil penalties, additional tax assessments, referrals to the Small Business/Self-Employed Division fraud technical advisors for further or joint investigation, and referrals to Criminal Investigation, the Federal Bureau of Investigation, or other law enforcement agencies for criminal prosecution.
 - D. Identified other processes used by ADAPT management to assess its impact to stem the growth of fraudulent and abusive activities in the Indian tribal sector.
 - E. Evaluated whether ITG office management had set program goals and measured program performance against those goals to stem the growth of fraudulent and abusive activity in the Indian tribal sector.
- II. Identified actions taken by the ADAPT to stem the growth of fraudulent and abusive activities in the Indian tribal sector since FY 2008.
 - A. Determined whether ITG office management established processes for encouraging referrals from internal and external sources that relate to ADAPT goals.

¹ Pub. L. No. 103-62, 107 Stat. 285 (codified as amended in scattered sections of 5 U.S.C., 31 U.S.C., and 39 U.S.C.).

² A 12-consecutive-month period ending on the last day of any month, except December. The Federal Government's fiscal year begins on October 1 and ends on September 30.



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- B. Determined whether ADAPT management established procedures for screening and classifying referrals received from internal and external sources and only accepting those meeting the goals of the program.
- C. Evaluated examination inventory for all employees assigned to the ADAPT and determined whether all cases assigned to ADAPT examiners met program acceptance criteria.
- D. Determined whether the ADAPT coordinated with Criminal Investigation, the Small Business/Self-Employed Division, or any other agency or professional organization to stem the growth of abusive activities or fraud.

Internal controls methodology

Internal controls relate to management's plans, methods, and procedures used to meet their mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance. We determined the following internal controls were relevant to our audit objective: ITG office policies, procedures, and practices for encouraging, screening, and classifying referrals; case acceptance criteria; and methods for monitoring and measuring performance to stem the growth of fraudulent and abusive activity in the Indian tribal sector. We evaluated these controls by interviewing ITG office management, reviewing ADAPT examination inventory, reviewing the Government Performance and Results Act of 1993, and reviewing other applicable documentation.



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Appendix II

Major Contributors to This Report

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*Fraud and Abuse Are Addressed in the
Indian Tribal Sector, but Performance Objectives and
Measures Are Needed to Assess Program Effectiveness*

Appendix III

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Appendix IV

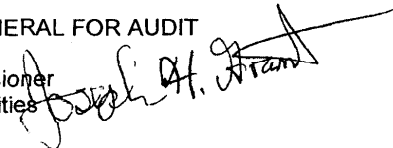
Management's Response to the Draft Report



**DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224**

January 9, 2013

MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM: Joseph H. Grant, Acting Commissioner
Tax Exempt and Government Entities 

SUBJECT: "Fraud and Abuse Are Addressed in the Indian Tribal Sector,
but Performance Objectives and Measures Are Needed to
Assess Program Effectiveness"

Thank you for your review of our Abuse Detection and Prevention Teams (ADAPT) and for your suggestions for improving the program. We appreciate your detailed observations and recommendation.

The Indian Tribal Governments Office (ITG) has the unique role of interacting with sovereign tribal governments on federal tax matters. The ADAPT groups specifically focus on the areas of fraud and tax avoidance schemes in Indian Country. In this role, ADAPT receives referrals from multiple sources, including tribal members, elected officials, employees, and tribal law enforcement. We consider the tribes our partners in combating those abuses, and ADAPT works along with other law enforcement, including tribal law enforcement, to protect tribal assets from abuse or exploitation.

Your report acknowledges the progress we have made in implementing ADAPT since your last review in 2003, and it recommends additional improvements related to performance objectives and measures. Our response to your recommendation is found in the attachment.

Before coming to that, however, we wish to make several observations.

The first concerns the parenthetical statement on page 6 of the report that tribal members examined were related to 12 percent of Federally-recognized tribes. Our experience, and the data we have seen, does not support any implication that fraudulent or abusive schemes are more prevalent in Indian Country than in other sectors of the population, or that tribes or their members are the major source of those schemes.



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The second concerns the definition of the term "tax module," discussed in the report at footnote 18. The example given relates to individual Forms 1040 and is not illustrative of the examinations ADAPT conducts, which are primarily examinations of entities. In that context, the concept of a tax module for employment tax purposes would be more instructive. One year of an employment tax exam generally involves six tax modules. Thus the numbers in Figure 1 of the report would generally need to be divided by six to get an estimate of the number of tax years involved. We also would like to emphasize that the number of tax modules examined does not in any way reference the number of tribal entities examined. It is very common for an examination to involve multiple years on one entity. Accordingly, Figure 1 cannot be read to relate to the number of tribal entities examined.

Our final observation is that ADAPT's work to combat tax avoidance schemes in Indian Country is appropriate and necessary. The majority of referrals that ADAPT accepts for examination involve business entities, rather than individual tribal members, and the necessity of this work is shown by a change rate in closed ADAPT examinations that is close to 100%.



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Attachment

Recommendation: The Director, ITG, should develop specific performance objectives for the ADAPT, along with associated measures, to better assess how effectively the program is addressing fraud and abuse in the Indian tribal sector.

Corrective Action: ITG will review the performance objectives and associated measures in other IRS fraud-related programs to determine whether, and at what level, similar standards can be implemented by ADAPT. To the degree appropriate, ITG will then implement such standards.

Implementation Date: ITG will complete its review of performance objectives and associated measures by June 30, 2013. It will complete any subsequent implementation by September 30, 2013.

Responsible Official: Director, Indian Tribal Governments Office