

**BEFORE THE
U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON WAYS AND MEANS
SUBCOMMITTEE ON OVERSIGHT**

Hearing on Protecting Small Businesses

From IRS Abuse, Part II

May 25, 2016

10:00 a.m.

Rayburn House Office Building

Room B318

Testimony of Robert Everett Johnson

Good morning, Chairman Roskam, Ranking Member Lewis, and Members of the Committee. I am pleased to have the opportunity to talk to you about the issue of civil forfeiture, and specifically the IRS's use of so-called "structuring" laws to take money from small business owners who are guilty of nothing more than depositing money at the bank.

I am an attorney at the Institute for Justice, a public-interest law firm that litigates to protect property rights nationwide. I represent Randy Sowers—also testifying today—in his effort to recover funds taken by the IRS under the structuring laws.

I previously testified before this Committee in February 2015, and at that time the IRS had recently issued a change of policy designed to protect small business owners from abuse under the structuring laws. At that hearing, IRS Commissioner Koskinen apologized to individuals who were wrongly targeted for forfeiture merely because of their bank deposits.

Today, over one year later, the government still has not corrected its abuse of the structuring laws. The government has not returned money that was seized and forfeited *before* its policy change. Randy Sowers has filed a petition asking the government to return \$29,500 seized in May 2012, and the government has not answered that petition although more than 10 months have gone by since it was filed.

More than 600 individuals—who together had over \$43 million taken by the IRS because of how they deposited or withdrew money from the bank—also continue to wait for some measure of justice.

At the same time, small business owners *continue* to face persecution at the hands of federal prosecutors because of their bank deposits. Vocatura's Bakery, a third-generation family business located in Norwich, Connecticut, had over \$68,000 seized by the IRS in May 2013 under the structuring laws. The government has now held the Vocaturas' money for over three years without bringing its case before a judge—violating statutory deadlines set by Congress as well as internal DOJ policies. Just recently, in February 2016, the government pressured the Vocaturas to plead guilty to *criminal* structuring charges and to agree to forfeit both the initial \$68,000 seized by the IRS as well as an additional sum of approximately \$160,000. When the Vocaturas refused, federal prosecutors retaliated by serving the Vocaturas with an overbroad grand jury subpoena seeking *eight years* of almost every financial record generated by the business.

In short, much remains to be done. Property owners like Randy Sowers are still waiting to get back money that never should have been seized in the first place. And others, like the Vocatura family, continue to face IRS agents and federal prosecutors who want to take their money—and even put them in prison—because of how they deposit their hard-earned money in the bank.

Structuring: The Law Of Bank Deposits

As the Committee is by now well aware, so-called “structuring” laws criminalize everyday financial transactions that most Americans would never think could be a crime.

Federal law requires banks to file a currency transaction report with the U.S. Department of the Treasury for any cash transaction in excess of \$10,000 (an amount that has not been adjusted for inflation since first being set in the 1970s, when \$10,000 was equivalent to over \$60,000 today).¹

Federal structuring law, meanwhile, makes it unlawful for a bank customer to break up cash deposits or withdrawals into amounts below that \$10,000 threshold “for the purpose of evading” federal currency reporting.² A person who has violated this latter prohibition is said to have impermissibly “structured” cash transactions.

These laws were intended to target drug dealers and other hardened criminals engaged in money laundering or other criminal activity. In practice, however, the IRS has enforced the structuring laws against innocent Americans who have no idea that depositing cash in the bank could possibly get them in trouble with the law. For instance:

¹ 31 U.S.C. § 5313

² 31 U.S.C. § 5324.

- In August 2013, Carole Hinders, the proprietor of Mrs. Lady’s Mexican Food, a small-town restaurant in Spirit Lake, Iowa, had more than \$32,000 seized by the IRS—the restaurant’s entire bank account.³ Years ago, Carole’s mother told her that depositing more than \$10,000 created a hassle for the bank. Carole had no idea that trying to make life easier for the bank might be a federal crime. After first attempting to pressure Carole to agree to forfeit a portion of the money, the IRS finally agreed to return all of Carole’s money sixteen months after the seizure.
- In March 2013, Mark Zaniewski, the proprietor of Metro Marathon service station, in Sterling Heights, Michigan, had his business’s entire bank account—over \$33,000—seized by the IRS.⁴ An IRS agent advised Mark that he should go ahead and deposit any additional funds belonging to Metro Marathon into the account to avoid bouncing checks to his vendors. Mark borrowed \$10,000 from his sister-in-law and also made additional deposits of credit card receipts into the account. Then, in early April 2013, the IRS seized all this newly deposited money (over \$37,000) from the account. Although Mark often deposits cash in

³ See *United States v. Thirty-Two Thousand Eight Hundred Twenty Dollars and Fifty-Six Cents in U.S. Currency*, No. 13-CV-4102 (N.D. Iowa).

⁴ See *United States v. Thirty-Three Thousand Two Hundred Forty-Four Dollars and Eighty-Six Cents in U.S. Currency*, No. 13-cv-13990 (E.D. Mich.).

amounts under \$10,000, he also sometimes deposits more than \$10,000; this pattern reflects the fact that he goes to the bank every few days to deposit cash to cover vendor bills and to safeguard surplus cash. Eight months after the seizure, the IRS finally agreed to return the money.

- In May 2012, Jeffrey, Richard, and Mitchell Hirsch, the proprietors of Bi-County Distributors, Inc., had over \$446,000 seized by the IRS—once again, the entire contents of their business’s bank account.⁵ The Hirsch brothers were advised by their own accountant to keep cash deposits under \$10,000 to reduce paperwork burdens for their banks, as banks today often close the accounts of customers that make frequent large cash deposits. The IRS held the Hirsch brothers’ money for thirty-two months, over two-and-a-half years, and repeatedly sought to negotiate a settlement under which the brothers would agree to forfeit a significant portion of the money. Finally, however, after the case attracted media scrutiny, the IRS agreed to return the money in full.

In all these cases, the individuals targeted by the IRS had no interest in concealing their activities from the government; each had a legitimate purpose for their banking practices. None of these individuals was ever

⁵ See *In the Matter of the Seizure of Four Hundred Forty Six Thousand Six Hundred Fifty One Dollars and Eleven Cents in U.S. Currency*, No. 14-mc-1288 (E.D.N.Y.).

accused of any crime other than depositing cash in the bank in amounts under \$10,000. Yet the government seized their money without warning and without asking any questions prior to the seizure. Then, the government forced them to fight for months or years to get their money back.

Shockingly, when the IRS engages in such tactics, it can use the money that it takes to pad its own budget. When the IRS uses civil forfeiture to take money for structuring violations, the money is deposited in the Treasury Forfeiture Fund.⁶ By law, the assets in the Treasury Forfeiture Fund are available “without fiscal year limitation” for use by the Secretary of the Treasury to fund the law enforcement activities of the IRS and other agencies within the Treasury Department—including to fund additional seizures.⁷ In other words, the money that the IRS takes from hardworking Americans can be put back to work to seize money from *additional* Americans.

In response to significant and negative press attention, including a front-page article in the *New York Times*, the IRS announced in October 2014 that it was adopting a new policy under which it would only pursue structuring cases where the money came from an illegal source. The DOJ adopted a similar policy in March 2015. These policy changes apply to both

⁶ See U.S. Dept. of Treasury, Treasury Executive Office for Asset Forfeiture, <http://1.usa.gov/1XrLor5>.

⁷ 31 U.S.C. § 9703(a).

civil and criminal forfeitures and are designed to prevent these types of cases from occurring in the future. But these policy changes are not binding on the agencies and could be reversed at any time. They also fail to provide meaningful legal protection, as they do not provide a statutory defense to property owners wrongly targeted for forfeiture. And, of course, these changes do nothing at all to help the hundreds of property owners who had their property taken before IRS and DOJ announced their policy changes.

The Government Continues To Harass Small Business Owners
Because Of Their Bank Deposits

Notwithstanding the IRS and DOJ policy change announcements, the government today continues to harass small business owners in the name of enforcing the structuring laws.

When this Committee last met to discuss this issue, in February 2015, Representative Holding asked the Commissioner of the IRS about a case in which the government was continuing to seek the forfeiture of more than \$107,000 taken from Lyndon McLellan, the owner of a convenience store in Robeson County, North Carolina.⁸ Commissioner Koskinen responded, “If that cases exists, then it’s not following the policy.” Yet, when the responsible federal prosecutor was informed about this exchange, he responded with an

⁸ See *United States v. \$107,702.66 in United States Currency*, No. 7:14-cv-295 (E.D.N.C.).

email stating that he was “concerned” that details about the case had been provided to Congress. He went on:

Whoever made [the documents] public may serve their own interest but will not help this particular case.

Your client needs to resolve this or litigate it. But publicity about it doesn't help. It just ratchets up feelings in the agency.

My offer is to return 50% of the money. The offer is good until March 30th COB.⁹

The Institute for Justice subsequently took over as counsel for Lyndon in the forfeiture case. The government agreed to return the seized money *in full* despite having just recently demanded 50% of the funds—but only after the case received significant attention in the press.

Since that time, the government has continued to harass another small business—Vocatura's Bakery, in Norwich, Connecticut—because of a pattern of under-\$10,000 bank deposits. As in Lyndon's case, the seizure of the business's funds occurred prior to the IRS and DOJ policy changes, but the government has continued to seek the forfeiture of the funds even after the policy changes were announced.

Vocatura's Bakery is a third-generation family business. The current owners grew up in the bakery and can tell you stories about playing there as

⁹ A copy of this email is available online at <http://ij.org/r/wp-content/uploads/2015/05/westemail.pdf>.

kids. Today, they work around the clock to keep the bakery going. The baking is done mostly at night, and then the fresh bread is sold throughout the day. The Vocaturas do significant cash business at their retail store, and for years they made frequent under-\$10,000 cash deposits at the bank.

On May 1, 2013, a group of armed IRS agents and a U.S. Marshal showed up without advance warning at the bakery. From the start, the government conducted the case as a fishing expedition: The Vocaturas report that the agents asked a series of outlandish questions, including whether they were dealing drugs or running a prostitution ring out of the bakery. Then, at the end of the raid, the agents informed the Vocaturas that the government had seized the bakery's entire operating account—over \$68,000—under the structuring laws.

During the three years that have passed since the seizure, the government has done *nothing* to prove its case to a judge. The government has simply held the Vocaturas' money and applied steadily mounting pressure to convince the Vocaturas to agree to “voluntary” forfeiture of the funds. This approach violates federal law, which requires the government to commence civil or criminal forfeiture proceedings within 150 to 180 days

following a seizure.¹⁰ This approach also violates DOJ's March 2015 policy announcement, which states that a federal prosecutor "must either file a criminal indictment or a civil complaint against the asset" within "150 days of a seizure based on structuring" absent specific approval from the relevant United States Attorney.¹¹

Notably, after IRS abuse of the structuring laws began to attract significant attention in the press, the government went over a year without contacting the Vocaturas about the seizure. Then, on February 18, 2016, the government sent two of the Vocatura brothers proposed *criminal* plea agreements, under which the brothers would have to agree to waive their right to indictment by a grand jury and plead guilty to structuring. Under the agreements, the Vocaturas would have agreed to forfeit the initial \$68,000 seized by the IRS as well as an *additional* approximately \$160,000 that could be taken from the brothers' personal assets. The brothers also would have faced anywhere from 37 to 46 months in prison.

¹⁰ 18 U.S.C. § 983(a). The government has 60 days to send notice of a seizure to the property owner, at which point the property owner has 30 days to file a claim to the property. After a claim has been filed, the government has 90 days to either file a civil forfeiture proceeding or obtain a criminal indictment containing allegations that the property is subject to forfeiture.

¹¹ A copy of the DOJ's policy change memorandum is available at <http://1.usa.gov/1W8Mzg2>.

The Vocaturas rejected the government's proposed plea agreements, as they feel they have done nothing wrong. In response, one might have thought that the government would carry through with its threat of prosecution by seeking a criminal indictment. But the government did nothing of the sort. Instead, the responsible federal prosecutor informed the Vocaturas that, if they did not plead guilty to structuring, he would launch a criminal tax investigation into their business.

On May 10, 2016, the prosecutor followed through with his threat and served the Vocaturas with an incredibly overbroad grand jury subpoena seeking *eight years* of practically every record generated by the business. The subpoena demands the following for the period between January 1, 2008 and the present:

All books, general ledgers, records, bank statements, cancelled checks, deposit tickets, work papers, financial statements, correspondence, Form W-2's and Form 1099's issued, payroll records for any and all employees, list of employees with addresses and contact information, records of suppliers and distributors, cash receipts journals, and other pertinent documents furnished by or on behalf of [Vocatura's Bakery] for the preparation of state and federal tax returns and for any other entity in which [the owners of Vocatura's Bakery have] a financial interest . . .

All records, books of account, and other documents or papers relative to financial transactions of [Vocatura's Bakery] . . . [and]
...

All invoices, receipts, sales slips, and billing records for [the bakery's] clients/customers, including . . . all correspondence with this client/customer.

In other words, because the Vocaturas refused to agree to plead guilty to criminal charges of structuring, the government launched a fishing expedition into practically every aspect of the business—and launched this fishing expedition a full three years after the seizure of the bakery's money.

The IRS Still Holds Millions In Ill-Gotten Gains

At the same time that the government has continued to pursue forfeitures under the structuring laws, the government also has failed to return millions of dollars seized *before* the IRS and DOJ policy changes.

Through requests under the Freedom of Information Act, the Institute for Justice has obtained data from the IRS suggesting that the agency today holds tens of millions of dollars that it would not have seized under current policies. Between 2007 and 2013, the IRS forfeited about \$43 million in 618 cases in which the IRS reported no suspicion of criminal activity other than the mere fact of sub-\$10,000 cash deposits or withdrawals.¹²

In July 2015, the Institute for Justice launched an effort to recover money seized and forfeited under the structuring laws prior to the DOJ and

¹² See Dick M. Carpenter II, Ph.D and Larry Salzman, Institute for Justice, *Seize First, Question Later*, at 17 (2015). While *Seize First* does not break down these specific figures, they are derived from the same data that forms the basis for Figure 3 in the report.

IRS policy changes.¹³ The Institute filed petitions on behalf of two property owners: Randy Sowers, also testifying today, and a North Carolina convenience store owner named Khalid Quran who had over \$150,000 taken because he withdrew money from the bank in amounts under \$10,000.

These petitions—termed “petitions for remission or mitigation”—were filed under a provision of federal law that allows the government to return money even after it has been permanently forfeited to the government.¹⁴ They are administrative filings—submitted to IRS or DOJ, rather than to a court—asking the government to voluntarily return money that it took through civil forfeiture. In many ways, they are akin to a petition seeking a presidential pardon, except for civil forfeiture rather than the criminal law. The government has discretion to grant a petition for remission or mitigation, and thus to return forfeited money, whenever it determines that granting the petition would advance the interests of justice.

Significantly, the fact that a property owner “voluntarily” agreed to the forfeiture of funds in a settlement does not bar the government from returning those funds in response to a remission petition. The DOJ’s *U.S. Attorneys’ Manual* explains that “[t]he remission and mitigation process, like

¹³ Information about this effort, including relevant documents and correspondence, may be found at <http://ij.org/case/structuring-petition/>.

¹⁴ See 19 U.S.C. § 1618; 31 U.S.C. § 5321.

the pardon process in criminal cases, is completely independent of the litigation and case settlement process.”¹⁵

Nor should the existence of such settlement agreements be used as an excuse to avoid returning forfeited money. Property owners often had little choice other than to agree to the forfeiture of their funds: The cost to litigate would frequently swamp the amount of money at issue, as half of all seizures under the structuring laws between 2005 and 2012 were of amounts under \$34,000.¹⁶ And, as the Sowers case demonstrates, property owners also had to contend with the threat that they would be subject to *criminal* sanctions or additional property seizures if they did not agree to give up their money. Against these considerations, the government frequently offered to return half or more of the seized money in exchange for a “voluntary” agreement to forfeit the remainder.

The government also plainly has the resources to return this money. While past structuring forfeitures that would violate current policies likely total around \$43 million for the period between 2007 and 2013, the Treasury Forfeiture Fund today contains a far larger amount. At the close of Fiscal

¹⁵ *U.S. Attorneys’ Manual* § 9-113.400, available at <http://1.usa.gov/20klvJd>; see also *id.* (“No agreement, whether a settlement in civil judicial action or a plea agreement resolving both criminal charges and the forfeiture of assets, may contain any provision binding the Department and the agencies to a particular decision on a petition for remission or mitigation.”).

¹⁶ *Seize First, supra*, at 10.

Year 2015, the fund had a net position of \$6.1 *billion*.¹⁷ According to an internal Treasury audit, the fund closed 2015 “with \$4.6 billion in Gross Non-Exchange Revenues and a total of \$806.6 million for FY 2014, reflecting two, highly successful revenue years.”¹⁸ Pursuant to federal statute, these billions of dollars in forfeited assets can be used to return money that was wrongly seized from property owners.¹⁹

The IRS has, in fact, already granted one of the two petitions filed by the Institute for Justice. On February 18, 2016, the IRS agreed to return all of the money taken from Khalid Quran. Because Khalid’s forfeiture was processed as an administrative forfeiture—meaning the settlement occurred before the government had to file a forfeiture complaint in federal court—Khalid’s petition was decided by the IRS. By contrast, because Randy’s forfeiture was processed as a judicial forfeiture—meaning that the settlement occurred *after* a forfeiture complaint was filed—his petition is addressed to DOJ and will be decided by the Chief of DOJ’s Asset Forfeiture and Money Laundering Section.²⁰ As of today, the only response that Randy has received to his petition is a May 9, 2016 letter from DOJ stating that the agency has

¹⁷ See Office of Inspector General, Department of the Treasury, *Audit of the Department of the Treasury Forfeiture Fund’s Fiscal Years 2015 and 2014 Financial Statements* (Feb. 2016), available at <http://1.usa.gov/1RgaySn>.

¹⁸ *Id.* at 12.

¹⁹ 31 U.S.C. § 9705(a)(1)(E); see also *id.* § 9705(f)(2)(I)(ii).

²⁰ See 28 C.F.R. § 9.1(b)(2).

received a recommendation from IRS as to how to rule on the petition and is in the process of considering its own response.

If the IRS could return the \$150,000 taken from Khalid Quran, there is no reason the government could not also return the \$29,500 taken from Randy Sowers. Indeed, there is no reason the government could not return the tens of millions of dollars wrongly taken from hundreds of other property owners under the structuring laws. The government would not take that money under current DOJ and IRS policies. Indeed, IRS Commissioner Koskinen apologized for taking that money when he testified before this Committee in February 2015. Now the government should do the right thing and give that money back.

The IRS Evades Public Scrutiny

At the same time that the government has continued to pursue forfeitures under the structuring laws and has delayed return of previously-forfeited money, the IRS also has resisted efforts to bring transparency to this area of the law.

On March 3, 2015, the Institute for Justice submitted a Freedom of Information Act request to the IRS, seeking access to an IRS database that tracks the seizure and forfeiture of assets by the agency. The Institute previously requested access to a similar database maintained by DOJ, and DOJ granted access to its database without charging any fee. That database

formed the basis for an important series of *Washington Post* articles exploring DOJ's use of civil forfeiture.²¹ The IRS, however, was not nearly as accommodating: It responded to the Institute's request for access to *its* database by seeking to charge the Institute a \$753,760 fee because it claims the Institute is a "commercial use requester" even though the Institute is a 501(c)(3) non-profit that publishes its research reports for free online and has no "commercial use" for the data. This three-quarters-of-a-million dollar fee is so large that it amounts to a denial of the request.

The Institute filed an administrative appeal with the IRS on December 14, 2015, asking the IRS to reconsider its decision. On January 8, 2016, the IRS sent a letter stating that the Institute has no right to appeal the decision imposing the fee because the decision "is not a denial" of the request. At the same time, the IRS has made clear that the decision imposing the fee is its "final response" to the FOIA request and that it is "closing [its] file in regard to this matter." This is straight out of Kafka: The IRS maintains that it can impose a three-quarters-of-a-million dollar fee for access to information and that there is no right to appeal such a determination.

As a result, the Institute for Justice still has not been granted access to the data that it seeks more than a year after making the FOIA request.

²¹ *Stop and Seize*, Washington Post, <http://wapo.st/1u6TICK>.

Further Reform Remains Needed

In light of the foregoing, it should be clear that further reform of the structuring laws remains desperately needed. Abuse of small business owners continues today, even after IRS and DOJ policy changes, and reform also is necessary to return money wrongly seized and forfeited in the past.

Among other things, Congress should:

- Eliminate the profit incentive that underlies this phenomenon by providing that property seizures by the IRS shall go to the general fund, rather than being available to the IRS to fund its operations.
- Codify IRS and DOJ policy changes by amending the legal definition of structuring to make clear that a person does not violate the structuring laws unless transactions are structured to conceal some other form of illegal activity. This would ensure that individuals have a judicial remedy in cases where IRS and DOJ do not follow their new policies.
- Enact legislation directing IRS and DOJ to return property that would not be seized under current IRS and DOJ policies for structuring cases.

While property can and should be returned via the remission and mitigation process, a legislative directive to return property would provide more concrete assurance that property will be returned.

- Provide individuals targeted for alleged structuring with a right to a prompt post-seizure hearing at which they may provide an explanation

for a pattern of under-\$10,000 deposits or otherwise contest the legality of the seizure.

- Create new reporting requirements to increase transparency. IRS should be directed to create a publicly-available database providing a real-time catalogue of seizures and forfeitures, as well as to issue periodic reports to inform Congress and the public about the agency's use of the forfeiture laws—including the types of forfeitures, the agencies involved, and the conduct that leads to forfeiture.

Conclusion

In closing, I want to thank the Committee for its continued interest and engagement in this topic. The Committee's actions—including the letters that the Committee has sent in support of property owners seeking return of wrongly-seized property—have played an important part in the progress that has already been made on this issue. I look forward to continuing to work with the Committee to secure justice for Americans wrongly targeted by the IRS under the structuring laws.

Thank you for the opportunity to testify.