

Internal Revenue Service
memorandum

date: March 31, 1997

to: Chief Inspector
National Office

from: Chief, Criminal Investigation Division [REDACTED]
South Texas District

subject: Possible Improprieties by Assistant Chief Counsel (Criminal Tax)

Re: Henry G. Cisneros
[REDACTED]

An administrative criminal tax investigation of Henry Cisneros was initiated in late 1994 after the media reported that he had allegedly lied to the FBI during a background investigation to finalize his confirmation as Secretary of Housing and Urban Development (HUD). The alleged false statements were in regard to the amount and frequency of payments he had made to his former mistress, Linda Jones Medlar. Medlar was also a political fund raiser for Henry Cisneros.

The Office of Independent Counsel (OIC) has conducted their own investigation and inquiry into matters related to Cisneros. OIC independently requested expansion authority to include possible tax violations from two separate sources, a three judge panel and Attorney General Janet Reno. The OIC request was made on January 28, 1997. They are currently awaiting the court's order on both requests.

On December 20, 1996, the Criminal Investigation Division (CI) forwarded a Special Agent's Report and related exhibits to District Counsel, Austin, Texas, with a recommendation that criminal proceedings be instituted against Cisneros. The criminal investigation disclosed that Cisneros willfully filed false Federal income tax returns for the years 1991, 1992, and 1993 in violation of Title 26, U.S.C., Section 7206(1).

After the prosecution case had been forwarded to District Counsel, several incidents occurred which have caused CI to be highly concerned about possible improprieties in the office of Assistant Chief Counsel (Criminal Tax). Specifically, our concerns are: (1) Barry Finkelstein is reported to have a very "cozy" relationship

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with Cisneros' defense counsel; (2) the case was pulled from the field with the apparent intent to "kill" it, regardless of the evidence and; (3) improper disclosures have possibly taken place with the Tax Division of the Department of Justice in a further attempt to stop the case from being prosecuted. Our observations and a discussion of these items are presented below:

1. Unprecedented Deviation from the Normal Review Process

The normal review process calls for the CI Chief to forward the prosecution case to District Counsel, after he/she concurs with the prosecution recommendation. If District Counsel concurs with the recommendation for prosecution; they then transmit the case to the Tax Division of the Department of Justice for their review.

James Macdonald, Assistant District Counsel, upon receipt of the Cisneros' case assigned District Counsel Attorney Thomas Eagan in Austin, Texas, to conduct the legal review. Eagan had substantially completed the review and had utilized Revenue Agent [REDACTED], detailed to District Counsel, to review the computations and method of proof. Macdonald was then contacted by Carl Knectel, Regional Counsel in Dallas, and requested to immediately furnish a copy of the Special Agent's Report (SAR) to Chief Counsel's Office in Washington, DC for their review.

Shortly thereafter, Macdonald notified CI that Chief Counsel had informed him they did not believe the case could be prosecuted. Chief Counsel stated there was double counting of income, errors in the special agents' computations, inappropriate method of proof, and an inability to establish willfulness on the part of Henry Cisneros. They also indicated a grand jury should have been utilized to tie down the witnesses. Chief Counsel's Office raised these concerns after only reading the SAR. Their determination had been made without any review of the exhibits, witness statements or analysis of the special agents' schedules.

→ Sometime on or before January 15, 1997, District Counsel was informed by Chief Counsel's Office that the case was to be transferred to the National Office. District Counsel was told this was necessary due to the sensitive nature of the case, which required a "centralized review." District Counsel was directed to cease their review, box up the exhibits and the report and mail it to Chief Counsel.

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I am not aware of any other criminal tax cases that have been pulled from experienced District Counsel attorneys to be reviewed in Washington. It should be noted that District Counsel, based upon their review of the evidence and involvement in the case as it was being investigated, was supportive of the prosecution recommendation.

2. Apparent Failure to Consider Facts and Evidence

The decision to decline this case seems to have been made regardless of the evidence and facts. At the very beginning of the process, Barry Finkelstein, having only read the SAR, had also contacted National Office CI officials indicating the case could not be prosecuted due to the wrong method of proof being utilized, errors in computations and lack of evidence.

It is highly questionable and baffling as to why Chief Counsel's Office decided to extract a "sensitive" case from an experienced District Counsel, and assign the legal review to two attorneys (Martin Klotz and Martin Needles) who do not review criminal tax cases on a regular basis.

Martin Klotz informed the CI Group Manager and Special Agents that he did not have any accounting background and was relying on Martin Needles to conduct the financial analysis. Klotz further explained Chief Counsel recently hired Needles, and the Cisneros' case was his first case to review. Based upon the discussions the group manager and the special agents had with Klotz and Needles regarding methods of proof, it was apparent that neither attorney understood or had previous exposure with the bank deposits method of proof. It was also apparent that they had received their direction to kill this case from Barry Finkelstein at the outset.

Barry Finkelstein was never present during any of the meetings held to discuss the evidence. However, Martin Klotz constantly referred to "Barry this" and "Barry that." It is our concern that the Office of Assistant Chief Counsel (Criminal Tax), and Barry Finkelstein in particular, has not based the decision to decline this case on the facts and evidence.

In an effort to address the concerns and questions raised by Chief Counsel, CI flew the group manager and two case agents to Washington. On January 28, 1997, these three individuals met with Klotz and Needles. The manager and two special agents walked through the entire SAR and

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evidence with Klotz and Needles. Klotz and Needles indicated to CI that all of their questions had been answered to their complete satisfaction, and they saw no errors in the computations or serious flaws in the case. However, after their ~~subsequent~~ discussion with Finkelstein on the morning of January 29, 1997, they reverted back to their original position that the case could not be prosecuted. Klotz indicated Finkelstein did not want to meet with the agents and that Finkelstein was the "deciding factor" regardless of what Klotz might think. Klotz then jokingly commented that he needed the job because his boys were in college. This comment has been interpreted to mean that Klotz has been directed by his superior and is fearful for his position.

Criminal Investigation requested, at the very least, to have the case returned for supplemental work to address any concerns Chief Counsel might have. Finkelstein refused to return the case.

There were a number of additional telephone discussions between Chief Counsel's Office and the investigating agents and group manager during the following weeks. The general purpose of these conversations was to answer questions and concerns raised by Counsel. In addition, a conference was held with defense counsel on February 12, 1997, wherein they presented to Chief Counsel their version of the events and their reasons why the government should not go forward with prosecution in this matter. CI did not receive a copy of this conference memo until March 7, 1997. A review of the conference memo disclosed that the defense submitted "a story" to Chief Counsel, which was an unfactual and unfounded version of the events. Chief Counsel immediately and wholeheartedly accepted the defense counsel view as the factual basis for declining this prosecution. They summarized their views in their memorandum dated March 7, 1997, and outlined their concerns with the case. This memorandum parrots the defense version and is replete with misstatements and false characterizations of the evidence and testimony.

In a final attempt to deal with the issues raised by Chief Counsel, the CI chief, group manager and one of the assigned special agents flew to Washington, DC. The Director of Investigations from Dallas joined them there for another meeting with Counsel. It should be noted that the original arrangement for this meeting was for Martin Klotz to fly to Austin. However, Finkelstein insisted that we "come to them" and thus forced four travelers to incur

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airfare costs and per diem, instead of just one.

In this meeting which took place on March 18, 1997, Criminal Investigation pointed out to Klotz and Needles every piece of evidence that rebutted the defense counsels' presentation of the "facts" and the points raised in the Counsel memorandum of March 7. This meeting was to no avail since Counsel officially declined the case in their memorandum dated March 27, 1997. Their declination is nothing more than an enhanced version of the March 7th memorandum and a regurgitation of the defense characterization of the facts. They clearly did not consider the points raised during the meeting of March 18.

In summary, Chief Counsel's Office has consistently failed to rely upon the evidence showing Cisneros' guilt. The evidence shows Cisneros was involved in his tax affairs, and knowingly concealed substantial income in each of three years from his CPAs and the Internal Revenue Service.

3. Chief Counsel's Relationship with Defense Counsel

It has been reported that Barry Finkelstein has a cozy and/or close relationship with defense attorneys Cono Namarato and Chad Muller. Both of these individuals have been retained by Cisneros to represent him in the matters at hand. This relationship apparently has existed for a number of years and perhaps dates back to the time that Namarato and Muller were employed by the Tax Division.

Throughout their involvement in this process, Chief Counsel has wholeheartedly accepted and endorsed the defense version of events. As mentioned previously, the "story" which has been created, quickly falls apart when compared to the facts, testimony and evidence gathered during the investigation. In addition, when they write about and discuss the case, Chief Counsel exaggerates and misstates events to bolster the position they have taken. Their discussion of the case mirrors the position put forth by Cisneros' defense attorneys. It is not objective and unbiased. Examples of this conduct abound and include the complete discounting of the evidentiary value of the recorded conversations between Cisneros and Medlar and the insistence that Cisneros was completely unaware of office activities and the manner in which income was recorded.

On January 8, 1997, Group Manager Sheila Colbenson was contacted by Chad Muller, one of Cisneros' defense

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attorneys. Muller requested a Chief's conference and indicated the agents had promised him an opportunity prior to forwarding the case to District Counsel (which was untrue). Muller indicated he had contacted District Counsel, and they did not have a problem with a District conference. It was explained to Muller the case had already been forwarded, and no conference would be held by Criminal Investigation at the District level. However, he could request a conference with District Counsel.

Sometime on or before January 15, 1997, District Counsel received notification to forward the complete SAR and exhibits to Assistant Chief Counsel. On January 21, 1997, Technical Assistant Martin Klotz informed the District of their concerns about the case. He also revealed Barry Finkelstein had agreed to a conference with defense counsel over a week earlier, and the conference had been scheduled for February 12, 1997. Therefore, it appears that Finkelstein had already agreed to and scheduled a conference with defense counsel prior to "taking" the case from District Counsel.

Another example of defense counsel's reliance on Finkelstein, is when the defense counsel made an oral and written request for the CPA's workpapers in order to prepare for the Chief Counsel conference. The District denied this request. The defense attorney's (Chad Muller) response was words to the effect " I'll just get those records from Chief Counsel then". Defense counsel sounded absolutely confident and assured that he would receive the documents and total cooperation from Chief Counsel's Office.

4. Chief Counsel's Disclosures to DOJ, Tax Division

In the meeting on March 18, 1997, Klotz explained to the Criminal Investigation Division that Stan Krysa, Department of Justice, Tax Division, had forwarded OIC's request to the Department of Justice for expansion of his investigation to include tax matters to Finkelstein. Krysa asked Finkelstein to review the request and give his opinion. Klotz stated Finkelstein opened the package and saw that it was grand jury material, he immediately closed the package and informed Krysa that he could not disclose anything related to a potential tax case, nor could he review the grand jury material.

However, District Counsel, Austin, Texas, recently informed Criminal Investigation Division that Stan Krysa,

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Department of Justice, Tax Division, had asked District Counsel about the case involving the "secretary". Krysa stated he believed the case was not prosecutable. Krysa indicated he had meet with Cisneros' defense counsel and the Public Integrity Section of the Department of Justice on February 12, 1997. The purpose of that meeting was to discuss the Office of Independent Counsel's request to Attorney General Janet Reno for expanded authority in its investigation of Henry Cisneros.

Krysa also indicated CID was "dragging its feet" in responding to Chief Counsel's conference memorandum so that OIC could take jurisdiction. When Krysa was asked who told him that, he said he couldn't remember.

OIC informed Special Agent Lange of Attorney General Reno's initial written response to OIC's expansion request. The language used in Reno's response mirrors the language Finkelstein has given to CID for declining the case.

It is District Counsel's opinion that Krysa seemed to have "inside" knowledge from Assistant Chief Counsel (Criminal Tax) about the review of the case. It also appears that the possible disclosure by Chief Counsel, of their intentions to decline the case, has potentially influenced Reno's decision. Her decision should have been made independently and without knowledge of any tax investigation.

In conclusion, we raise these issues for your consideration because we have serious concerns about the propriety of the actions that have taken place in the review of this case. We are not privy to nor do we wish to speculate about personal or political motivations for the conduct that we have witnessed. The Criminal Investigation Division will protest the declination of the case. However, we strongly feel that the conduct of Assistant Chief Counsel (Criminal Tax) which preceded this declination needs to be examined.

We are elevating our concerns with full appreciation of the gravity of this situation. Please feel free to call me at [REDACTED] if you have questions or need additional information. Members of your staff may call Group Manager Sheila Colbenson at [REDACTED]


John J. Filan