Tax evasion as the predicate offense of money laundering under German and US law

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Tax fraud is a common charge in both the US and Germany. It can also be the predicate offense for money laundering, although US law uses a detour to re-classify tax evasion as mail or wire fraud to have a named predicate offense. However, whereas proceeds of money laundering are usually a taken asset, most cases of tax evasion result in a kept one, with the saved expenditures stemming from unpaid taxes. This leads to problems to which the two jurisdictions have found their own solutions. For one problem, namely the proceeds in commingled bank accounts, some US courts have found a preferable solution. While the German courts seem to deem the entire bank account, including the white money, as tainted, some federal US courts apply a clean-funds-first-out rule to resolve fundamental concerns.

I. Introduction

In the public perception, money laundering is connected more closely to drug cartels than to international corporations. When it comes to these international corporations and global players, more public attention is paid to tax avoidance and tax structuring, especially through shell companies in tax havens. Shell companies can be used for all kinds of legal activities, but thanks to the possibility of anonymity and the absence of almost all reporting requirements, they also attract such illegal activities as hiding illegally obtained assets and/or legally obtained money from tax authorities.

The Panama Papers and, most recently, the Mauritius Leaks, revealed by the International Consortium of Investigative Journalists ("ICIJ"), uncovered a vast network of shell companies, their directors and owners. The key player in the Panama Papers was the Panamanian law firm Mossack Fonseca & Co., which advised numerous people on founding and administering offshore companies. In a significant amount of cases, these companies were using tax havens not only for tax structuring but also for tax evasion.

But what if tax evasion results in a risk of criminal conviction not only for the tax evaders but also for those who benefit – directly or indirectly – from the money hidden in offshore companies? If the money were simply hidden in an offshore firm structure, it would be quite useless. Therefore, it is crucial to move the offshore funds after the taxes are avoided, and to use the money for legitimate business transactions. Several methods have been employed in the past to do this. One example of a money laundering scheme is the Russian Laundromat, in which money from offshore accounts was used to buy products with long-term economic value, such as high-profile electronics or jewelry. Such products can be transported and sold easily and would be exported to countries where the suspect needed the money and where they would be sold. In this way, money was derived from ostensibly legal transactions. The purchasing costs were deducted, making it appear as though the money were from a legal source.

Using offshore funds in this way creates its own risk of criminal conduct. Once money is tainted, using it can constitute money laundering for all individuals who participate in these transactions and are aware of – or anticipate – the illicit origin.

One of the first indictments resulting from the Panama Papers, United States v. Ramses Owens et al[1], was recently filed before US courts. According to the indictment, Mossack Fonseca helped US taxpayers conceal income generated by assets and investments from the Internal Revenue Service (IRS) through a scheme of sham offshore companies. The charges include conspiracy to defraud the US, conspiracy to commit wire fraud, conspiracy to commit tax evasion, wire fraud, money laundering conspiracy, and others. The money laundering conspiracy charges are based on the claim that the defendants allegedly transported, transmitted, and transferred monetary instruments and funds internationally, "with the intent to promote the carrying on of specified unlawful activity […]."[2] The defendants involved are German, Panamanian, and US citizens.

The Panama Papers leak revealed shell companies owned by people all over the world. Prosecution offices worldwide are investigating whether those shell companies serve some illegal purpose, possibly tax evasion.

This case thus offers an opportunity to compare the crime of money laundering based on tax evasion in Germany and the US. It has long been taken for granted that tax evasion is placed alongside other crimes such as bribery or robbery as a predicate offense to money laundering in both the US and German judicial systems. A predicate offense is a crime that generates money which is subsequently laundered. However, tax evasion as a predicate offense has its own pitfalls, as the money laundering offense is tied to the tainted proceeds of the predicate offense. Such proceeds are obvious in a case of robbery: they are the taken property. But in a case of tax evasion, the defendant has kept something rather than taken it. Here, legally obtained assets of the defendant become proceeds if they are not declared as required under the tax laws. Therefore, tax evasion as the predicate offense raises the question, "What are the proceeds of the tax evasion?" Is it the entire money moved offshore tainted? Is the amount of saved expenditure tainted? Or do no proceeds arise in the first place?

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[1] See the indictment under https://www.justice.gov/usao-sdny/press-release/file/1117201/download (4.4.2020).

[2] Indictment in United States v. Ramses Owens et al, p. 60; the US taxpayer and the US accountant pleaded guilty in February 2020 and thus waived their right to a trial, see the press release by the DOJ from February 18, 2020, no. 20-199, and February 28, 2020, no. 20-252. They are scheduled to be sentenced on June 24 and June 29, 2020. The other both defendants, a German citizen and a Panamanian citizen, are not in the USA but facing charges in their home countries.

The next question arises in connection with commingled accounts: How does each jurisdiction determine whether tainted money is used if money is withdrawn from a bank account containing both legitimate and illicit sources?

II. Country report

First, we need to look at the money laundering statutes of each jurisdiction to understand the requirements.

§ 261 German Criminal Code – Money laundering; hiding unlawfully obtained financial benefits[3]

(1) Whosoever hides an object which is a proceed of an unlawful act listed in the 2nd sentence below, conceals its origin or obstructs or endangers the investigation of its origin, its being found, its confiscation, its deprivation or its being officially secured shall be liable to imprisonment from three months to five years. Unlawful acts within the meaning of the 1st sentence shall be

1. felonies;
2. misdemeanours under
   (a) Section 332 (1), also in conjunction with subsection (3), and section 334;
   (b) Section 29 (1) 1st sentence No 1 of the Drugs Act and section 19 (1) No 1 of the Drug Precursors (Control) Act;
3. misdemeanours under section 373 and under section 374 (2) of the Fiscal Code, and also in conjunction with section 12 (1) of the Common Market Organisations and Direct Payments (Implementation) Act;
4. misdemeanours
   (a) […];
   (b) under […] and section 370 of the Fiscal Code, […].

which were committed on a commercial basis or by a member of a gang whose purpose is the continued commission of such offences; and

5. misdemeanours under section 89a and under section 129 and section 129a (3) and (5), all of which also in conjunction with section 129b (1), as well as misdemeanours committed by a member of a criminal or terrorist organisation (section 129 and section 129a, all of which also in conjunction with section 129b (1)).

The 1st sentence shall apply in cases of tax evasion committed on a commercial basis or as a gang under section 370 of the Fiscal Code, to expenditure saved by virtue of the tax evasion, of unlawfully acquired tax repayments and allowances, and in cases under the 2nd sentence no 3 the 1st sentence shall also apply to an object in relation to which fiscal charges have been evaded.

(2) Whosoever

1. procures an object indicated in subsection (1) above for himself or a third person; or
2. keeps an object indicated in subsection (1) above in his custody or uses it for himself or a third person if he knew the origin of the object at the time of obtaining possession of it shall incur the same penalty.

(3) The attempt shall be punishable.

(4) In especially serious cases the penalty shall be imprisonment from six months to ten years. An especially serious case typically occurs if the offender acts on a commercial basis or as a member of a gang whose purpose is the continued commission of money laundering.

(5) Whosoever, in cases under subsections (1) or (2) above is, through gross negligence, unaware of the fact that the object is a proceed from an unlawful act named in subsection (1) above shall be liable to imprisonment of not more than two years or a fine.

(6) The act shall not be punishable under subsection (2) above if a third person previously acquired the object without having thereby committed an offence.

(7) Objects to which the offence relates may be subject to a deprivation order. section 74a shall apply. section 73d shall apply if the offender acts on a commercial basis or as a member of a gang whose purpose is the continued commission of money laundering.

(8) Objects which are proceeds from an offence listed in subsection (1) above committed abroad shall be equivalent to the objects indicated in subsections (1), (2) and (5) above if the offence is also punishable at the place of its commission.

(9) Whosoever

1. voluntarily reports the offence to the competent public authority or voluntarily causes such a report to be made, unless the act had already been discovered in whole or in part at the time and the offender knew this or could reasonably have known and
2. in cases under subsections (1) or (2) above under the conditions named in No 1 above causes the object to which the offence relates to be officially secured

shall not be liable under subsections (1) to (5) above.

Whosoever is liable because of his participation in the antecedent act shall not be liable under subsections (1) to (5) above, either.

The relevant US law is found in two sections under Title 18 (the code for Crimes and Criminal Procedures) of the U.S. Code (U.S.C.) § 1956 – Laundering of monetary instruments; and § 1957 – Engaging in monetary transactions in property derived from specified unlawful activity.[4]

[3] Cited https://www.gesetze-im-internet.de/englisch_stgb/ (4.4.2020), even though it is the most recent official translation, please note that this version is outdated and its latest amendment was in October 2013. An amendment that could affect the topic of this article is solely an additional § 261 (9) 3rd sentence. This excludes the impunity stipulated by § 261 (9) 2d sentences for defendants who bring the proceeds into circulation and in doing so conceal the criminal origin.

[4] Cited https://www.law.cornell.edu/uscode/text/18/1956 and https://www.law.cornell.edu/uscode/text/18/1957 (4.4.2020).

18 U.S. Code § 1956:

(a)

(1) Whoever, knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, conducts or attempts to conduct such a financial transaction which in fact involves the proceeds of specified unlawful activity –

(A)

(i) with the intent to promote the carrying on of specified unlawful activity; or

(ii) with intent to engage in conduct constituting a violation of section 7201 or 7206 of the Internal Revenue Code of 1986; or

(B) knowing that the transaction is designed in whole or in part —

(i) to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity; or

(ii) to avoid a transaction reporting requirement under State or Federal law,

shall be sentenced to a fine of not more than $ 500,000 or twice the value of the property involved in the transaction, whichever is greater, or imprisonment for not more than twenty years, or both. For purposes of this paragraph, a financial transaction shall be considered to be one involving the proceeds of specified unlawful activity if it is part of a set of parallel or dependent transactions, any one of which involves the proceeds of specified unlawful activity, and all of which are part of a single plan or arrangement.

(2) Whoever transports, transmits, or transfers, or attempts to transport, transmit, or transfer a monetary instrument or funds from a place in the United States to or through a place outside the United States or to a place in the United States from or through a place outside the United States –

(A) with the intent to promote the carrying on of specified unlawful activity; or

(B) knowing that the monetary instrument or funds involved in the transportation, transmission, or transfer represent the proceeds of some form of unlawful activity and knowing that such transportation, transmission, or transfer is designed in whole or in part –

(i) to conceal or disguise the nature, the location, the source, the ownership, or the control of the proceeds of specified unlawful activity; or

(ii) to avoid a transaction reporting requirement under State or Federal law,

shall be sentenced to a fine of not more than $ 500,000 or twice the value of the monetary instrument or funds involved in the transportation, transmission, or transfer, whichever is greater, or imprisonment for not more than twenty years, or both. For the purpose of the offense described in subparagraph (B), the defendant's knowledge may be established by proof that a law enforcement officer represented the matter specified in subparagraph (B) as true, and the defendant's subsequent statements or actions indicate that the defendant believed such representations to be true.

(3) Whoever, with the intent –

(A) to promote the carrying on of specified unlawful activity;

(B) to conceal or disguise the nature, location, source, ownership, or control of property believed to be the proceeds of specified unlawful activity; or

(C) to avoid a transaction reporting requirement under State or Federal law,

conducts or attempts to conduct a financial transaction involving property represented to be the proceeds of specified unlawful activity, or property used to conduct or facilitate specified unlawful activity, shall be fined under this title or imprisoned for not more than 20 years, or both. For purposes of this paragraph and paragraph (2), the term "represented" means any representation made by a law enforcement officer or by another person at the direction of, or with the approval of, a Federal official authorized to investigate or prosecute violations of this section.

(b) Penalties.

(1) In general. – Whoever conducts or attempts to conduct a transaction described in subsection (a) (1) or (a) (3), or section 1957, or a transportation, transmission, or transfer described in subsection (a) (2), is liable to the United States for a civil penalty of not more than the greater of –

(A) the value of the property, funds, or monetary instruments involved in the transaction; or

(B) $ 10,000.

[…]

(c) As used in this section –

(1) the term "knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity" means that the person knew the property involved in the transaction represented proceeds from some form, though not necessarily which form, of activity that constitutes a felony under State, Federal, or foreign law, regardless of whether or not such activity is specified in paragraph (7);

(2) the term "conducts" includes initiating, concluding, or participating in initiating, or concluding a transaction;

(3) the term "transaction" includes a purchase, sale, loan, pledge, gift, transfer, delivery, or other disposition, and with respect to a financial institution includes a deposit, withdrawal, transfer between accounts, exchange of currency, loan, extension of credit, purchase or sale of any stock, bond, certificate of deposit, or other monetary instrument, use of a safe deposit box, or any other payment, transfer, or delivery by, through, or to a financial institution, by whatever means effected;

(4) the term "financial transaction" means (A) a transaction which in any way or degree affects interstate or foreign commerce (i) involving the movement of funds by wire or other means or (ii) involving one or more monetary instruments, or (iii) involving the transfer of title to any real property, vehicle, vessel, or aircraft, or (B) a transaction involving the use of a financial institution

which is engaged in, or the activities of which affect, interstate or foreign commerce in any way or degree;
(5) the term "monetary instruments" means (i) coin or currency of the United States or of any other country, travelers' checks, personal checks, bank checks, and money orders, or (ii) investment securities or negotiable instruments, in bearer form or otherwise in such form that title thereto passes upon delivery;
(6) the term "financial institution" includes […]
(7) the term "specified unlawful activity" means
(A) any act or activity constituting an offense listed in section 1961(1) of this title except an act which is indictable under subchapter II of chapter 53 of title 31;
(B) with respect to a financial transaction occurring in whole or in part in the United States, an offense against a foreign nation involving—
(i) […]
(iii) fraud, or any scheme or attempt to defraud, by or against a foreign bank (as defined in paragraph 7 of section 1(b) of the International Banking Act of 1978)); [1]
(iv) bribery of a public official, or the misappropriation, theft, or embezzlement of public funds by or for the benefit of a public official;
(v) smuggling or export control violations involving – […]
[…]
(8) the term "State" includes […]
(9) the term "proceeds" means any property derived from or obtained or retained, directly or indirectly, through some form of unlawful activity, including the gross receipts of such activity.
(d) Nothing in this section shall supersede any provision of Federal, State, or other law imposing criminal penalties or affording civil remedies in addition to those provided for in this section.
(e) Violations of this section may be investigated by […]
(f) There is extraterritorial jurisdiction over the conduct prohibited by this section if—
(1) the conduct is by a United States citizen or, in the case of a non-United States citizen, the conduct occurs in part in the United States; and
(2) the transaction or series of related transactions involves funds or monetary instruments of a value exceeding $ 10,000.
(g) Notice of Conviction of Financial Institutions. […]
(h) Any person who conspires to commit any offense defined in this section or section 1957 shall be subject to the same penalties as those prescribed for the offense the commission of which was the object of the conspiracy.
(i)Venue. […]

18 U.S. Code § 1957:

(a) Whoever, in any of the circumstances set forth in subsection (d), knowingly engages or attempts to engage in a monetary transaction in criminally derived property of a value greater than $ 10,000 and is derived from specified unlawful activity, shall be punished as provided in subsection (b).
(b)
(1) Except as provided in paragraph (2), the punishment for an offense under this section is a fine under title 18, United States Code, or imprisonment for not more than ten years or both. If the offense involves a pre-retail medical product (as defined in section 670) the punishment for the offense shall be the same as the punishment for an offense under section 670 unless the punishment under this subsection is greater.
(2) The court may impose an alternate fine to that imposable under paragraph (1) of not more than twice the amount of the criminally derived property involved in the transaction.
(c) In a prosecution for an offense under this section, the Government is not required to prove the defendant knew that the offense from which the criminally derived property was derived was specified unlawful activity.
(d) The circumstances referred to in subsection (a) are—
(1) that the offense under this section takes place in the United States or in the special maritime and territorial jurisdiction of the United States; or
(2) that the offense under this section takes place outside the United States and such special jurisdiction, but the defendant is a United States person (as defined in section 3077 of this title, but excluding the class described in paragraph (2)(D) of such section).
(e) Violations of this section may be investigated by such components of the Department of Justice as the Attorney General may direct, and by such components of the Department of the Treasury as the Secretary of the Treasury may direct, as appropriate, and, with respect to offenses over which the Department of Homeland Security has jurisdiction, by such components of the Department of Homeland Security as the Secretary of Homeland Security may direct, and, with respect to offenses over which the United States Postal Service has jurisdiction, by the Postal Service. Such authority of the Secretary of the Treasury, the Secretary of Homeland Security, and the Postal Service shall be exercised in accordance with an agreement which shall be entered into by the Secretary of the Treasury, the Secretary of Homeland Security, the Postal Service, and the Attorney General.
(f) As used in this section—
(1) the term "monetary transaction" means the deposit, withdrawal, transfer, or exchange, in or affecting interstate or foreign commerce, of funds or a monetary instrument (as defined in section 1956(c)(5) of this title) by, through, or to a financial institution (as defined in section 1956 of this title), including any transaction that would be a financial transaction under section 1956(c)(4)(B) of this title, but such term does not include any transaction necessary to preserve a person's right to representation as guaranteed by the sixth amendment to the Constitution;
(2) the term "criminally derived property" means any property constituting, or derived from, proceeds obtained from a criminal offense; and
(3) the terms "specified unlawful activity" and "proceeds" shall have the meaning given those terms in section 1956 of this title.

Tax evasion is a criminal act under § 370 German Fiscal Code (tax evasion) and 26 U.S.C. § 7201 (attempt to evade or defeat tax).

III. Overview

To digest these complex norms, we can reduce them to their core for the purposes of the following comparison.

1. German law

a) Predicate offense – tax evasion

The money laundering statute in Germany contains a conclusive list of unlawful acts that are considered as predicate offenses. As stated above, Germany, like the US, regards tax evasion as a predicate offense.

The German Criminal Code names tax evasion (§ 370 German Fiscal Code) in the money laundering statute (§ 261 [1] [4] [b] German Criminal Code), but limits its scope to cases committed on a commercial basis, or by a member of an organized group[5] whose purpose is the continued commission of such offenses (here tax evasion). The simpler versions of tax evasion, which do not meet these standards, are not considered as sufficient for a predicate offense for money laundering.

Under § 370 German Fiscal Code, a punishment shall be imposed on any person who "furnishes the revenue authorities or other authorities with incorrect or incomplete particulars concerning matters that are relevant for tax purposes," or "fails to inform the revenue authorities of facts that are relevant for tax purposes when obliged to do so" where this results in understating taxes or deriving unwarranted tax advantages.[6] The attempted perpetration is punishable under § 370 (2) German Fiscal Code.

b) Characteristic elements of money laundering

For the characteristic elements, the statute distinguishes between subsection (1) for the concealment and obstruction and subsection (2) for acts to isolate proceeds.

aa) Concealment and obstruction

The characteristic element under § 261 (1) German Criminal Code is (1) hiding an object which is a proceed of an unlawful act listed in the 2nd sentence of subsection (1), (2) concealing its origin or (3) obstructing or endangering the investigation of its origin, its being found, its confiscation, its deprivation, or its being officially secured.

(1) Hiding

Hiding means to screen the proceeds from discovery by moving or protecting against immediate perception by special arrangements.[7]

(2) Concealment

To conceal means to make it more difficult to uncover the origin by fraudulent or other actions.[8] Whereas hiding focuses on the object itself, concealment focuses on the object's origin.[9]

The German Federal Court of Justice (Bundesgerichtshof – BGH) combines the hiding and concealment actions and describes both as a focused and specific action to make the proof of origin more difficult.[10]

(3) Obstruction or (specifically) endangering

"Obstruction" under § 261(1) German Criminal Code refers to actions to obstruct or specifically endanger

- the identification of the proceeds' origin,
- proceeds being found,
- the confiscation,
- the deprivation,
- or the proceeds being officially secured.

bb) Isolation

The characteristic elements under § 261 (2) German Criminal Code refer to proceeds as mentioned in § 261 (1) German Criminal Code and prohibits the isolation of such proceeds, in particular procuring such proceeds for oneself or a third person, keeping such proceeds in one's custody, or using the proceeds for oneself or a third party. "Using" means any disposition or any proper disposal. The variants of keeping or using the proceeds are outlawed only if the defendant knew the origin of the object at the time of obtaining possession of it.

cc) Self-laundering

As stipulated in § 261 (9) 2nd sentence German Criminal Code, self-laundering is in general not a prosecutable offense. Self-laundering means that the defendant is the one who committed the predicate offense. This impunity, stipulated by § 261 (9) 2nd sentence German Criminal Code, is excluded for a defendant who brings the proceeds into circulation and in doing so conceals the criminal origin.

[5] The translation of the German Criminal Code calls the organized form a "gang." To avoid any association to street gangs, this paper uses the word "organized group." A gang/organized group under German criminal law means a group of at least three people whose purpose is the continued commission of such offenses (see BGH, Judgment of 3.3.2001 – GSSt 1/00 = BGHSt 46, 321).

[6] Cited https://www.gesetze-im-internet.de/englisch_ao/englisch_ao.html#p2615 (4.4.2020); the third criterion is omitted as irrelevant for this article.

[7] *Nestler/El-Ghazi*, in: Herzog (ed.), Geldwäschegesetz, Kommentar, 3rd ed. 2018, StGB § 261 para. 91; *Altenhain*, in: Kindhäuser/Neumann/Paeffgen (eds.), Nomos Kommentar, Strafgesetzbuch, 3rd Vol., 5th ed. 2017, § 261 para. 102.

[8] *Nestler/El-Ghazi* (fn. 7), StGB § 261 para. 91.

[9] *Nestler/El-Ghazi* (fn. 7), StGB § 261 para. 91.

[10] BGH, Judgment of 27.7.2016 – 2 StR 451/15 = NStZ 2017, 28 (29).

c) Proceeds in cases of tax evasion

In general, under the money laundering statute in § 261 German Criminal Code, proceeds are items that derive from ("herrühren") a predicate offense.[11] The specific meaning of "herrühren" in the context of § 261 German Criminal Code is not entirely clear. The legislature intentionally did not define the term, but there is consensus that some kind of causal relationship must exist between the property received out of the unlawful act and the proceeds.[12]

This would cover only those cases of tax evasion in which a tax amount would actually be refunded, because only in such cases is something obtained from the tax authorities. The legislature has recognized this problem, and thus the money laundering statute, § 261 (1) 3rd sentence, expressly stipulates that "[t]he 1st sentence shall apply in cases of tax evasion committed [...], to expenditure saved by virtue of the tax evasion, of unlawfully acquired tax repayments and allowances". Consequently, the proceeds in tax evasion cases are usually the amount of saved taxes based on the fact that those are not declared.

d) Intent

The German Criminal Code contains the general norm that "[u]nless the law expressly provides for criminal liability based on negligence, only intentional conduct shall attract criminal liability", § 15 German Criminal Code.

Money laundering is no exception. Each element of the crime must be fulfilled with intent. This is not a specific intent requirement, however. It is enough that the defendant willingly or knowingly acts in a certain way and mindfully accepts the outcome ("billigend in Kauf nehmen"). However, some voices in the literature read a specific intent into the variant of concealment.[13]

Regarding the knowledge of the criminal origin, the defendant is required to know the specific circumstances which, from a correct lay perspective, would constitute a predicate offense.[14] In addition, § 261 (5) German Criminal Code extends the criminal liability to cases in which the defendant is, "through gross negligence, unaware of the fact that the object is a proceed from an unlawful act" but reduces the sentences that can be imposed in such cases. It is noteworthy that the gross negligence is sufficient only with regard to the criminal origin, not to the act itself. The act needs to meet the "billigend in Kauf nehmen" requirement.

2. US law

a) Predicate offense – tax evasion

The US law defines as tax evasion the willful attempt in every matter to evade or defeat any tax imposed by the Internal Revenue Code or the payments thereof (26 U.S.C. § 7201).

The predicate offenses are such as stated under 18 U.S.C. § 1956 (c) (7) as well as RICO[15] crimes, as stated in § 1961 (1) as incorporated by § 1956 (c) (7) (A). In US law, predicate offenses are called "specified unlawful activities". Tax evasion, as a crime under 26 U.S.C. § 7201 (and § 7206), is not named as a specified unlawful activity, neither under 18 U.S.C. § 1956 (c) (7) nor under the RICO provisions.

The predicate offenses are not to be confused with the wording of § 1956 (a) (1) (A) (ii), which names tax evasion as its own variant of money laundering. Under 18 U.S.C. § 1956, tax evasion is not named as a predicate offense but instead considered as one specific intent (§ 1956 (a) (1) (A) (ii)) with which money could be laundered.

However, the US Department of Justice (DOJ) has stated that even though tax crimes are not named in the list of specified unlawful activities, the list does include mail fraud, see 18 U.S.C. § 1956 (a) (7) (A) incorporating § 1961 (1).[16] This means, from a practical point of view, that tax evasion can almost entirely turn a tax crime into a predicate offense for money laundering in the form of mail and wire fraud. An example of this can be found in United States v. Pasquantino.[17]

In practice, the US Attorney's Offices often bring tax evasion charges as mail or wire fraud. This is because under the internal revenue laws, the Tax Division of the DOJ must approve all criminal charges, including tax evasion, that a US attorney brings or intends to bring against a defendant, see 28 C.F.R. § 0.70 and Title 6, 4.200 Justice Manual (Criminal Tax Case Procedures).

The Wire Fraud statute of 18 U.S.C. § 1343 prohibits "any scheme or artifice to defraud, or for obtaining money or property by means of false or fraudulent pretenses, representations, or promises, transmits or causes to be transmitted by means of wire, radio or television communication in interstate or foreign commerce." Mail fraud, 18 U.S.C. § 1341 is the use of the postal system instead of a telecommunications system to effectuate a scheme or artifice to defraud. Dissenting Justice Scalia described the wire fraud in the Pasquantino hearing in a vivid matter as "using the mails [sic] or interstate commerce to defraud a […] government of taxes" in such cases.[18]

The defendant in United States v. Pasquantino argued that unassessed tax claims are neither property nor money, and

[11] While the official translation (see fn. 1) uses only the term "proceeds", the German text uses the term "herrühren" which means "stem from" or "derive from."

[12] BGH, Judgment of 18.2.2009 – 1 StR 4/09 = BGHSt 53, 205 (209).

[13] *Nestler/El-Ghazi* (fn. 7), StGB § 261 para. 126.

[14] BGH, Judgment of 17.7.1997 – 1 StR 791/96 = BGHSt 43, 158; BGH, Judgment of 18.1.2003 – 1 StR 393/02 = wistra 2003, 260; *Nestler/El-Ghazi* (fn. 7), StGB § 261 para. 127.

[15] Racketeer Influenced and Corrupt Organization Act, 18 U.S.C. §§ 1961-1968.

[16] DOJ 2012, Criminal Tax Manual, p. 3; applies also to wire fraud and bank fraud, see Tax Division Directive 128.

[17] Pasquantino v. United States, 125 S. Ct. 1766 (2005).

[18] https://www.oyez.org/cases/2004/03-725 (4.4.2020); Justice Scalia partially joined the dissent in this case.

therefore he could not be tried under the wire fraud statute. However, the court disagreed. The entitlement to collect money from petitioners is "something of value" belonging to the government and therefore is within the meaning of "property."[19] As such, tax crimes are predicate offenses because they also satisfy the requirements of the specified unlawful activity of mail, wire, or bank fraud.

This scheme has also been used in United States v. Ramses Owens et al. The named predicate offense is the charged wire fraud, not the charged tax evasion. The alleged fraudulent scheme, however, concealed the "assets and investments, and the income generated by those assets and investments, from the IRS" and was "[…] transmitted and caused to be transmitted interstate and foreign wires, including emails and bank wires, for the purpose of executing this fraudulent scheme".[20]

b) Characteristic element of money laundering (actus reus)

The characteristic element under § 1956 (a) (1) is a financial transaction conducted with specific intent.

The actus reus of money laundering is, therefore, the financial transaction in § 1956 (a) (1).[21] The term is defined in § 1956 (c) (3) and (4) and is completed by a wide list of rulings by various courts. Simply described, it can be almost any transaction of money or titles. The simple handover of drug proceeds to a courier[22] or the mere receipt of a client's cash bag by an attorney is sufficient.[23]

The defendant must conduct the transaction. Conduct is defined in § 1956 (c) (2) as initiating, concluding, or participating in initiating or concluding the transaction. The mere acceptance of receiving the funds in a transaction satisfies the participation in a conclusion element.[24]

c) Proceeds (in cases of tax evasion)

The requirement of "proceeds" is not part of the actus reus in the money laundering crime but rather a "circumstance element".[25] The property subject to the financial transaction must be the proceeds of the specified unlawful activity. As such, the illicit origin must not be known to the defendant generally, unless the law requires such knowledge.

As defined in § 1956 (c) (7), "the term 'proceeds' means any property derived from or obtained or retained, directly or indirectly, through some form of unlawful activity, including the gross receipts of such activity." Proceeds are broadly defined and do not need to be money; neither is it necessary that these proceeds are traceable to the predicate offense.[26] The government must show only that the proceeds came from the offense.[27] In this way it is sufficient to show that the legitimate business is bankrupt to prove that the money used must be the proceeds of the predicate offense.[28]

In the case of tax evasion, the "unpaid taxes, unlawfully disguised and retained through the mailing of the tax forms, were 'proceeds' of defendants' overall scheme to defraud the government".[29]

d) Intent (mens rea)

For the mens rea requirement, a distinction must be made between the money laundering statutes.

Almost[30] all money laundering variations require knowledge of the fact that the property involved is derived from some crime, not necessarily a crime defined as a specified unlawful activity.

At the same time, the forms of actions under § 1956 (a) must be fulfilled with their own set of specific intents. The mens rea requires a specific intent as stated in the rule § 1956 (a) (1). This can occur if the defendant intends to: aa) promote the specified unlawful activity, (A) (i); bb) evade taxes, (A) (ii), cc) conceal or disguise (B) (i), or dd) avoid transaction reporting requirements, (B) (ii).

aa) Promote

The defendant must act with the intent to promote a specified unlawful activity. This can involve the proceeds generated from a specified unlawful activity or a completely different crime. It is not required that the defendant conceal or disguise anything.[31] For example, the reinvestment in more drugs[32] or the renting of rooms to store and pack cocaine[33] has been seen as a promoting act.

[19] Pasquantino v. United States, 125 S. Ct. 1766 (2005).
[20] Indictment in United States v. Ramses Owens et al, p. 59.
[21] United States v. Roy, 375 F.3d 21 (1st Cir. 2004).
[22] United States v. Reed, 77 F.3d 139, 142 (6th Cir. 1996).
[23] Unites States v. Blair, 661 F.3d 755, 764 (4th Cir. 2011).
[24] United States v. Gotti, 459 F.3d 296, 335 (2d Cir. 2006).
[25] United States v. Mikell, 163 F. Supp. 2d 720, 739.
[26] See *Levy*, Federal Money Laundering Regulation, § 20.11 as to whether and when the term "proceeds" refers to net profits rather than the gross receipts and the application of United States v. Santos, 553 U.S. 507 (2008); Solved for the period after May 20, 2009 by the Congress response P.L. 111-21, 123 Stat. 1618 (2009) (S. 386) (111th Cong.) which gave the current definition including "gross receipts". Congress thus takes the broad definition.
[27] United States v. Mankarious, 151 F.3d 694 (7th Cir. 1998).
[28] United States v. Richardson, 658 F.3d 333, 338 (3d Cir. 2011).
[29] United States v. Yusuf, 536 F.3d 178 (3d Cir. 2008).
[30] The "international promotion offense" § 1956 (a) (2) (A) does not require any origin of the property used but rather the intent to promote a specified unlawful activity.
[31] United States v. Marbella, 73 F.3d 1508, 1514 (9th Cir. 1996); see also United States v. Alerre, 430 F.3d 681, 693 (4th Cir. 2005) for the difference between promoting a Specified Unlawful Activity and concealment.
[32] United States v. Fitzgerald, 496 Fed. Appx 175 (3d Cir. 2012).
[33] United States v. Cole, 558 Fed. Appx. 173 (3d Cir. 2014); such costs for a legitimate reason would not satisfy the "promoting" requirement.

bb) Evade taxation

Also, taking part in a financial transaction with the intent to engage in conduct that would trigger the tax evasion statutes 26 U.S.C. § 7201 or § 7206 constitutes money laundering.[34] Any tax which could be evaded satisfies the statute.[35] As mentioned above, this should not be confused with tax evasion as a predicate offense. Here, it is used as the motive of the financial transaction rather than the origin of the funds.

The intentional conduct must, in fact, violate tax laws. The defendant is not required to be aware that his or her conduct violates tax law.[36]

cc) Conceal or disguise

The defendant also launders money if he or she acts with the purpose of concealing or disguising the nature, location, source, ownership, or control of the proceeds derived from the specified unlawful activity. The government must prove that there is "a specific intent to structure a transaction so as to conceal the true nature of the proceeds".[37] The simple deposition or transportation of proceeds is not sufficient. As the Supreme Court held in Cuellar v. United States[38], hiding money in a vehicle in order to transport it tells us something about the manner in which the money is transported but does not reveal the purpose of transporting it. In this case, the defendant transported $ 81,000 towards the Mexican border, hidden under goat hair in his car. The court reversed the conviction because the government was not able to prove that the purpose of the transportation was to conceal or disguise the money but rather it was simply transported in a concealed manner.

The concealment variant of money laundering can be understood as the classic way of laundering money by disconnecting the proceeds from their origin and providing the appearance of legitimate wealth instead.[39]

For the intent requirement, it is also sufficient that someone else besides the defendant has the intent to conceal, and the defendant knows this.[40]

dd) Avoid transaction reporting requirements

The fourth mens rea variation is to design the transaction in a way that avoids reporting requirements such as the Currency Transaction Report (for CTR, transactions of more than $ 10,000), the Currency and Monetary Instrument Report (CMIR, common carrier transports more than $ 10,000), or the IRS/FinCEN Form 8300 currency reporting (businesses receiving cash payments exceeding $ 10,000).

e) Other money laundering statutes[41]

§ 1956 (a) (2) makes it unlawful to transport, transfer, or transmit funds into or out of the US with the specific intent to promote a specified unlawful activity, or with knowledge that funds are proceeds of unlawful activities, and with knowledge that the transportation, transfer, or transmission is done with the purpose of concealing or avoiding transaction reporting. This statute prohibits the international transportation or transmission of funds to promote a specified unlawful activity but does not require proceeds of such.

The so-called "Sting Provision" of § 1956 (a) (3) requires basically the same intent as § 1956 (a) (1) (except for § 1956 [a] [1] [A] [ii]), but the belief that this transaction involves proceeds of a predicate offense satisfies this statute regardless of whether the money does indeed derive from any predicate offense.

The alternative of § 1957 ("Spending Statute") prohibits the knowing engagement in a monetary transaction exceeding $ 10,000 if the funds are criminally derived from a specified unlawful activity. Violations of § 1957 and § 1956 work in tandem and are often charged together.[42]

f) State law examples

So far, only the federal law has been presented here, which applies only if the federal government has the jurisdiction. The federal government has the jurisdiction to regulate interstate commerce, Art. I § 8 of the United States Constitution. That means some effect on interstate commerce is a required element of the federal money laundering crime.[43]

If this element is not met, only state law applies. Almost all states in the US have their own statute punishing money laundering[44] in addition to the state money transmission laws.

[34] See for an example of the intent requirements United States v. Zanghi, 189 F.3d 71 (1st Cir. 1999).

[35] DOJ 2012, Criminal Tax Manual, p. 4.

[36] United States v. Zanghi, 189 F.3d 71 (1st Cir. 1999).

[37] United States v. Gilliam, 975 F.2d 1050, 1056 (4th Cir. 1992); see also United States v. Millender, Case No. 1:16-cr-239-1 (AJT) (E.D. Va. Sep. 21, 2018), here the court dismissed the concealment charges.

[38] Cuellar v. United States, 553 U.S. 550 (2008); applied to § 1956 (a) (1) (B) (i) by United States v. Huezo, 546 F.3d 174 (2d Cir. 2008).

[39] Even though this is not the only way to satisfy this requirement as clarified in *Cuellar v. United State*, 553 U.S. 550 (2008).

[40] United States v. Richardson, 658 F.3d 333, 340 (3d Cir. 2011).

[41] For more information see *Doyle*, Money Laundering: An Overview of 18 U.S.C. § 1956 and Related Federal Criminal Law, November 30, 2017, available at https://fas.org/sgp/crs/misc/RL33315.pdf (4.4.2020).

[42] *Brickery/Taub*, Corporate and White Collar Crime, 6th ed. 2017, p.615.

[43] See also United States v. Evans, 272 F.3d 1069, 1081 (8th Cir. 2001); United States v. Aramony, 88 F.3d 1369 (4th Cir. 1996).

[44] Examples: California Cal. Penal Code §§ 186.9, 186.10; Delaware Del. Code Ann. Tit. 11, § 951; Florida Fla. Stat. Ann. §§ 896.101 to 896.108; Illinois Ill.Comp. An. ch. 720 § 5/29B-1; Michigan Mich Comp. Laws Ann. §§ 750.411j to 750.411q; New Jersey N.J. Stat. Ann. §§ 2C:21-23 to 2C:21-29; New York N.Y. Penal Law §§ 470.00 to 470.25; Penn-

For the purposes of comparison, this article focuses on the federal laws, because even a minimal effect on interstate commerce satisfies the interstate commerce requirement.

IV. Comparison

Both the German and the US provisions give rise to a complex combination of the predicate offense, act, and intention or knowledge while acting. Both jurisdictions deem it necessary to include tax evasion as a predicate offense, despite the regulatory obstacles such as inclusion causes. We will now turn to responses and basic solutions to different fields of conflicts arising from tax evasion as a predicate offense.

1. Tax evasion as a predicate offense

Even though both jurisdictions consider tax evasion as a predicate offense for money laundering, they demand their own characteristic elements of the crime.

a) Qualifications

As we have seen, US law, on the one hand, does not mention tax evasion as a predicate offense but instead brings it in through the back door by considering tax evasion – or rather tax fraud – as mail, wire, or bank fraud, which are named as specified unlawful activities. German law, on the other hand, limits the scope of tax evasion to a certain level of perpetration (committed commercially or as a member of an organized group).

By limiting the relevant levels of perpetration, German law perceptibly reduces the number of cases of money laundering that can be committed with tax evasion as a predicate offense. It excludes the committing of tax evasion from every other form other than on a commercial basis or as a member of an organized group whose purpose is to continue to commit evasion. At the same time, it seems that US law does not see money laundering as a follow-on crime for tax evasion, while in fact applying it to much simpler forms of perpetration than German law does; in particular, money laundering fulfills the required elements of either mail fraud, wire fraud, or bank fraud. Considering that tax returns are usually filed by mail or – more frequently – electronically, almost all investigations into tax fraud may provide evidence to pursue the related fraud charges of mail or wire fraud, in connection with fraudulent tax returns.

Unlike the German money laundering statute, US law does not limit its scope to fraud reaching a certain level of criminal energy. The reasoning behind the German approach is that charges of money laundering are intended to target organized crime rather than ordinary criminals. US law intends to target organized crime as well, but the US criminal statutes are normally broader and prefer to provide an extended discretionary power to the prosecutors.[45] Thus, US prosecutors may drop charges if deemed inappropriate. German law, in contrast, obligates German prosecutors to file charges if the elements of a crime are fulfilled and negate discretion in this context. Consequently, German law must be designed with a more narrow scope.

b) Intent requirement

The intent requirement varies between the two jurisdictions.

Under US law, the conduct must have a specific intent in order to fulfill the money laundering requirement. German law, in contrast, may require some kind of specific intent for the concealment variant of the statute, as described above, but otherwise general intent is sufficient.

Concerning the knowledge of the criminal origin, a conflict exists between the fact that only a limited number of criminal acts can generate proceeds under the money laundering statute. At the same time, the defendant often lacks forethought into the specific criminal act the proceeds are derived from and, even more so, the necessary legal knowledge to relate the source to a specific crime. The jurisdictions respond differently to this issue.

The knowledge requirement is stricter in Germany than in the US when it comes to the specific criminal act the proceeds originated from. US law does require knowledge of the source. However, to know that the source is an illegal activity of any sort fulfills the requirement; it does not need to be a named specified unlawful activity.[46] Under German law, besides the grossly negligent ignorance, the defendant must know that the proceeds originated from a predicate offense named in the statute. However, the standard is an evaluation of the specific circumstances from a layperson's perspective and is moderated in this way. German law balances the stricter requirement by additionally outlawing grossly negligent ignorance of the criminal origin. Here, the German legislature established a novelty with the money laundering statute. It is unusual in German law that any kind of negligence is sufficient to fulfill the elements of an economic crime. Nonetheless, the lawmakers deemed it sufficient that the defendant is unaware of the criminal origin due to gross negligence.

Ultimately, when it comes to the sufficient level of intent, the two jurisdictions are quite similar in that they require the defendant only to see and accept the result of his or her conduct. Under German law, this is referred to as "assenting acceptance" ("billigend in Kauf nehmend")[47] while US law refers to it as being "willfully blind".[48]

sylvania 18 Pa. Cons. Stat. Ann § 5111; Texas Tex. Penal Code Ann. §§ 34.01 to 34.03; Washington Wash. Rev. Code Ann. §§ 9A.83.010 to 9A.83.04.

[45] *Kadisch/Schulhofer/Barkow*, Criminal Law and its Processes, 10th ed., Chapter 1 B. 3.

[46] United States v. Huezo, 546 F.3d 174, 183 (2d Cir. 2008).

[47] *Nestler/El-Ghazi* (fn. 7), StGB § 261 para. 126.

[48] United States v. Flores, 454 F.3d 149, 156 (3d Cir. 2006); United States v. Rivera-Rodriguez, 318 F.3d 268, 271 (1st Cir. 2003); *Podgor/Henning/Israel/King*, White Collar Crime, 2d ed. 2018, § 12.4.B.2; see also Global-Tech Appliances, Inc. v. SEB, S.A., 131 S.Ct. 2060, 2070-2071 (2011) for the details on this requirement.

2. Determination of proceeds

Defining the proceeds of tax evasion is not as clear-cut as it might seem at first glance.

a) Definitions

Under US law, as mentioned above, the "unpaid taxes, unlawfully disguised and retained through the mailing of the tax forms, were 'proceeds' of defendants' overall scheme to defraud the government".[49]

German law, in contrast, defines the proceeds of tax evasion as "expenditure saved by virtue of the tax evasion" § 261 (1) 3rd sentence German Criminal Code. The wording uses the German term "durch", which can also be translated as "through", thus requiring some form of causal connection.

b) Description of the problem

In a nutshell, US law defines the proceeds as a retainer, and German law as expenditure saved.[50] Both jurisdictions find the solution by defining the proceeds as something not really obtained but rather retained or saved through the unlawful act. If the taxes had been properly filed, a certain amount would have been paid to the treasury. This amount would no longer be available to the defendant, so it is deemed proceeds.

Even though these solutions are necessary to include the tax evasion in the series of predicate offenses for money laundering (without being limited to obtained reimbursements), they are incoherent. The necessary step to justify the chosen solutions of the two jurisdictions is the idea that if the tax had been filed properly, the tax authorities would automatically have collected the tax. But this is just the start of the problem. In the case of larceny, the obtained item is obvious. The item taken from the victim can be separated out of all items in possession of the thief. Even if money was taken, the banknotes could be isolated and identified, for example, by the serial number.

The unassessed tax claim, on the other hand, is not a consequence of a criminal act. Evading the assessment of taxes or even the willful non-payment of taxes does not change tax imposed by law. The tax claim is just incorrectly assessed. If the defendant had filed the taxes correctly, the same amount of taxes would be imposed as is the case after the tax evasion is revealed. If a person is subject to a tax rate of 20 % and he or she does not declare $ 100,000 in income, the taxes imposed on this income by law do not change; they still amount to $ 20,000. It is only that the amount could not be assessed. After the tax evasion is revealed, the tax claim of $ 20,000 will be assessed and enforced. The tax claim depends on the tax-related circumstances defined by the national tax provisions, thus the law imposes the claim independently whether an evasion occurred or not. The fact that tax evasion is prohibited does not change the character of the tax claim itself and no tax is imposed because of the evasion. In consequence, the unpaid taxes are not connected with the crime. The saving of these taxes is neither obtained through the evasion[51] nor retained through the sending of the tax form.

The term "through" stipulates some form of causal connection. One might ask what the proceeds would be if the defendant were not able to pay the taxes in any way. If the defendant is indigent at the moment the taxes would have become due if he or she had filed the taxes properly, then, under the German definition, no expenditure would be saved through the unlawful act because he or she could not have paid this expenditure if these taxes had been properly assessed. Under the US law definition, there is nothing the defendant could retain at all, so no proceeds would exist. Neither the German nor the US courts have solved any case in this way so far.

If we have a defendant who disguises income of $ 100,000 and taxes would be saved, what part of this income constitutes the unpaid taxes? If the income is paid into an offshore account and the due taxes are usually paid from a domestic bank account, the savings would most likely occur in the domestic bank account because that is where the taxes would have been paid from. While the "bad" money is hidden abroad and untouched, the domestic money would be tainted. However – at least when it comes to tax evasion as a predicate offense – the money moved abroad for the purpose of supporting the crime of tax evasion would most likely be considered tainted money.

The problem is inherent in the criminality of money laundering. Tainted money is taken and is supposed to become clean by disconnecting it from its illicit origin. The basis is a "something," the tainted money. This "something" can be followed through its dynamic laundering steps, either by transferring, replacing, or some other activity. The success of tax evasion is a non-assessed tax claim, thus a "nothing." In this way, we try to follow a "nothing" by becoming a "something." It is merely speculative to replace a "nothing" by a "something in thought" towards a real "something".[52]

Even if we accept this and assume that the non-assessed tax claim is a "something", we have another problem that Samson pointed out:[53] the timing. The starting point of any examination of causality is the origin. The origin must predate the success. If a launderer uses the money he or she has stolen, we know that this is the case because it occurs in real life. We could see that the banknote is taken, possessed and eventually used. The receiving moment comes before the

[49] United States v. Yusuf, 536 F.3d 178 (3d Cir. 2008).

[50] This term is justifiably criticized in the literature, for example *Samson*, in: Hirsch/Wolter/Brauns (eds.), Festschrift für Günter Kohlmann zum 70. Geburtstag, 2003, p. 263 (270), as being inherently contradictory.

[51] Please note that the German legislative material, BT-Drs. 14/7471 says that § 261 (1) 3rd sentence shall ensure that property is included which obtained in a clear connection with the tax crime rather than merely being acquired as a result of the tax crime itself. Even if such an explanation clarified anything, however, the law text uses the term "through", which cannot be replaced by the legislative material.

[52] For the German law see *Samson* (fn. 50), p. 272.

[53] See *Samson* (fn. 50), p. 273.

using moment because the illegal conduct leads to possession. In the case of saved expenditures or retained property, the not-using of the money to pay the potential tax is not a certain conduct in real life which can be determined in time and place. In cases of a tax bill in which the evaded tax would have been included, the time, at least, can be determined. It is the moment the tax bill is paid because at that moment also an even higher tax bill would have been paid, most likely. In other cases, it can even be uncertain whether the taxpayer would have paid at all if he or she were waiting for foreclosure action. Other uncertainties can also arise. Here the moment of possession occurs before the illicit act. At some point of the possession, parts of the possessed money switch their status and become tainted.

The third problem, as implied in the examples above, is that it is impossible to determine which part of the possessed assets is the saved expenditures, or which part of a higher amount would be the illegally retained part. For example, a defendant disguises $ 100,000 and invests $ 50,000 in real estate right away. Later he does not declare his taxes correctly, with the result that $ 20,000 of taxes are wrongfully not assessed. Would the real estate be tainted? No, because at the moment the real estate was acquired, the used money was untainted. There is no good reason why this result should differ just because the money was kept together and not invested.

Both jurisdictions circumvent this problem by defining a portion of the money arbitrarily as tainted. This tainted part of the asset can be determined in its value but cannot be located within the assets of the defendant. The proceeds could be any financial portion of the assets. As a result, any financial transaction from a bank account could satisfy the money laundering statute. In consequence, the entire money in any bank account of the defendant would be blocked if he or she wants to avoid money laundering.

Neither jurisdiction has found a coherent definition to determine the proceeds from a tax crime when no funds are reimbursed. This is understandable and shows that the criminal act of tax evasion is inconsistent with the crime of money laundering. On the one hand, money laundering is usually based on assets obtained through crime. The actual proceeds of tax evasion, on the other hand, are kept as part of a possession, rather than obtained. The tax claim still exists, but it is not assessed. If the tax evasion is exposed and the tax claim assessed, this tax claim is not based on the criminal act of tax evasion but rather on the income (legally) earned in the first place, regardless of whether it is declared or not. If it was declared as legally required, the same tax claim would exist.

c) Commingled bank accounts

However, both jurisdictions acknowledge tax evasion as a predicate offense and so the above-mentioned matters have additional consequences for the level of confiscation,[54] and for the question of whether tainted funds were used. For both questions, it must be determined what happens when legitimate funds become commingled with dirty money.

In the US this has become a key question in cases under § 1957 (the "Spending Statute") in recent years. As we have seen, this provision prohibits the knowing engagement in a monetary transaction exceeding $ 10,000 if the funds are criminally derived from a specified unlawful activity. When is the money used actually derived from a specified unlawful activity if a portion of the money is retained? The most relevant situations involve bank accounts.

When the tax savings are determined to be proceeds of tax evasion, the question arises of whether the entire bank account is infected by the now tainted savings. For example, the defendant has $ 1,000,000 in his or her bank account and unlawfully retained $ 50,000 in taxes which cannot be assessed by the tax authorities based on the defendant's fraudulent conduct. Now the defendant makes a payment of $ 100,000 from the same account. Are proceeds of the tax evasion used? If so, which part is tainted?

Various positions can be taken:

- The legitimate money is used first, so no proceeds are used (analogous to FIFO – first in, first out);
- The tainted money is used first, so $ 50,000 is legitimate and $ 50,000 is proceeds (analogous to LIFO – last in, first out);
- A part in proportion to the legitimate money is used, so $ 5,000 (5 % of the account balance because the saved taxes correspond to 5% of the money in the account) is proceeds and $ 95,000 is not (pro-rata); or
- As an extreme position, dirty money infects the entire bank account, so the entire $ 1,000,000 becomes tainted as soon as it comes into contact with the dirty money. Therefore, any use of the bank account is the use of proceeds.

The correct handling of such cases is currently under discussion in Germany. The Federal Court of Justice (Bundesgerichtshof, BGH) has issued a number of rulings in recent years in which it found that all funds in an account are seen as one item.[55] If now tainted money is deposited into a bank account, the entire money in the account becomes tainted as long as the deposited money is not, from an economic point of view, completely irrelevant in relation to the legitimate money in the account.[56] Transferring this ruling to the standard of the saved expenditure as applied in cases of tax evasion, the entire property of a tax evader would be tainted immediately, and thus virtually useless. To date, no higher court has decided on such a case and the ruling has not yet been applied to a controversial case, but some opinions in the

[54] 18 U.S.C. §§ 981, 982 or §§ 73–76c German Criminal Code, respectively.

[55] BGH, Judgment of 20.5.2015 – 1 StR 33/15 = NStZ 2015, 703; confirmed in BGH, Judgment of 12.7.2016 – 1 StR 595/15; BGH, Judgment of 15.8.2018 – 5 StR 100/18; BGH, Judgment of 27.11.2018 – 5 StR 234/18.

[56] BGH, Judgment of 20.5.2015 – 1 StR 33/15 = NStZ 2015, 703; BGH, Judgment of 12.7.2016 – 1 StR 595/15 = NStZ 2017, 167.

literature agree with the court's position.[57] However, many others disagree.[58] Tainting the entire money in the bank account could have a severe impact on the economy. Entire liquid funds of an entity or an individual would be useless as soon as they come in contact with tainted money and the person concerned knows or anticipates the illicit origin. This would happen even if the money was transferred against the will of the person concerned but he or she fails to take immediate action. If a business were exposed publicly with evasion, it would have to be cut out of the market because no other business could accept its money without also running the risk of money laundering and having its own funds tainted. As mentioned, the Federal Court of Justice has not yet ruled on a controversial case of this kind, so the matter has not been conclusively decided.

Some federal courts in the US have rejected the position taken by the German Federal Court of Justice. The Fourth Circuit took a similar position back in 1994,[59] but in more recent decisions the Fifth Circuit rejected the view that commingled funds could automatically be seen as tainted.[60] The Fourth Circuit reasoned that "the illicitly-acquired funds and the legitimately-acquired funds (or the respective portions of the property with each) cannot be distinguished from each other" once the funds become combined in one single asset.[61] Thus, the funds "cannot be traced to any particular source, absent resort to accepted, but arbitrary, accounting techniques".[62] In consequence, the funds from lawful activities are also tainted if commingled with the proceeds of illegal conduct. Later, the Fifth Circuit (as well as the Ninth Circuit) rejected this point of view by arguing that it cannot be proven beyond a reasonable doubt that the used money is tainted or obtained by illegal activities if the individual withdrawal is less than the amount of clean money in the account.[63] But "when the aggregated amount withdrawn from an account containing commingled funds exceeds the clean funds", the withdrawal contains tainted money even though it might be less than the amount of clean money in the account.[64] This alternative version to the first-in-first-out rule is named the clean-funds-out-first rule.[65] The clean funds are used first and the proceeds are used once the (aggregated) withdrawals exceed the amount of money in the clean funds. The clean-funds-out-first standard was recently confirmed in a case involving a conviction of counts of money laundering in violation of § 1957, even though the challenge on this ground was rejected.[66]

Other circuits have eschewed the clean-funds-first-out rule and instead adopted a plain standard. The matter regularly arises in cases of violation of § 1957 because here more than $ 10,000 in tainted money must be used. The Second Circuit, for example, recently held that a jury may find that a withdrawal contains more than $ 10,000 in tainted money if the commingled account contains more than $ 10,000 in tainted money in total, regardless of how much clean money is in the account.[67]

Although the federal courts are split and have not applied a uniform standard here, the IRS apparently does adopt the clean-funds-first-out rule in its evaluation – with one exception. Its Internal Revenue Manuals[68] note:

> "Defendants often commingle SUA proceeds with legitimate funds. The government need not prove that all proceeds in a transaction were unlawfully derived but must be able to trace some of the proceeds to a SUA. Criminally derived proceeds deposited with legal funds are considered to be withdrawn last unless the account/business is deemed to be *permeated with fraud*. This implies that the business operations are so intertwined with fraud that to segregate the legitimate operation and profits is impossible. Special agents should work closely with the attorney for the government when investigations involve commingled funds to ensure the elements of the crime are met."

The clean-funds-first-out rule is preferable because it takes into account that the burden of proof is on the government and not on the defendant who uses tainted money, as well as the fact that the burden of proof in criminal cases is "beyond a reasonable doubt".[69] The basic problem of how to handle commingled funds exists under both US and German jurisdictions. The author would welcome if the German courts opened a comparable discussion to that of the US federal courts and adopted a standard similar to the clean-funds-out-first standard.

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[57] *Fischer*, Strafgesetzbuch mit Nebengesetzen, Kommentar, 67th ed., 2020, § 261 para. 10, 9.

[58] See *Joecks*, in: Joecks/Jäger/Randt, Steuerstrafrecht, Kommentar, 8th ed. 2015, AO § 369 para. 219; *Nestler/El-Ghazi* (fn. 7), StGB § 261 para. 77, with further references in para. 76 and 77.

[59] United States v. Moore, 27 F.3d 969 (4th Cir. 1994).

[60] United States v. Loe, 248 F.3d 449 (5th Cir. 2001) referring to United States v. Davis, 226 F.3d 346, 357 (5th Cir. 2000); see also United States v. Rutgard, 116 F.3d 1270,1292 (9th Cir. 2000).

[61] United States v. Moore, 27 F.3d 969 (4th Cir. 1994).

[62] United States v. Moore, 27 F.3d 969 (4th Cir. 1994).

[63] United States v. Loe, 248 F.3d 449 (5th Cir. 2001).

[64] United States v. Davis, 226 F.3d 346, 357 (5th Cir. 2000).

[65] United States v. Evans, No. 17-20158 & No. 17-20159 U.S. App. Lexis 15785 (5th Cir. 2018), designated for publication; also named "drugs in, last out" rule, United States v. Rutgard, 116 F.3d 1270,1292 (9th Cir. 2000).

[66] United States v. Evans, No. 17-20158 & No. 17-20159 U.S. App. Lexis 15785 (5th Cir. 2018), designated for publication.

[67] United States v. Silver, 864 F.3d 102 (2d Cir. 2017).

[68] https://www.irs.gov/irm (4.4.2020), last reviewed or updated: June 20, 2019, part 9 "Criminal Investigation;" 9.5.5.2.1. 5.1.

[69] See United States v. Loe, 248 F.3d 449 (5th Cir. 2001); "beyond a reasonable doubt" standard is quite similar in Germany, see BGH, Judgment of 1.7.2008 – 1 StR 654/07; BGH, Judgement 30.7.2009 – 3 StR 273/09.

This standard is transferable to tax evasion cases. The amount of unassessed taxes can be seen as the 'grounds' of a bank account, like the coffee grounds in a cup of coffee. It becomes the grounds at the moment the tax is (under)assessed or would be assessed if properly filed. As long as the grounds remain untouched and no withdrawal is made from the bank account, only clean funds are used. In the example above, no money laundering would have occurred because at least $ 900,000 remained in the account, which is more than the retained $ 50,000 in tainted money. The grounds remain untouched and are not used.

However, this does not solve the problem that occurs if the defendant has more than one bank account. If the defendant in the example above holds $ 100,000 in each of 10 bank accounts and makes a payment of $ 100,000 from one account, the question is whether the grounds are shared equally between the 10 accounts and each account contains $ 5,000 of tainted funds, or whether only the most recently touched bank account is tainted with $ 50,000, or whether the bank account usually used in the past to pay taxes is tainted.

The saved expenditures usually occur in the account from which the potential cost would have been paid. The tax payment would usually come from one particular account, not split across multiple accounts. Therefore, the saved expenditures would remain in one account and aggregate there.

This may change when offshore accounts are involved. The lay perspective would assume that the 'dirty' money was shifted offshore. While the domestic funds, as well as the funds moved offshore, are legally obtained, the money moved offshore makes the tax evasion possible and complicates the discovery of the evasion and the administration of justice. Therefore, it would be justified to deem the offshore funds as tainted.

3. The sentencing of tax evaders and money launderers

We will now turn briefly to the consequences of committing tax evasion or money laundering in each jurisdiction.

Both tax evasion and money laundering damage general welfare. Whereas the tax evader withholds money from the treasury, the money launderer uses assets derived from illegal activities, thus undermining legal financial transactions with illicit funds and complicating the reclamation of the proceeds and the administration of justice.

Under US federal law, money laundering, as stated in 18 U.S.C. § 1956 (a) (1), can carry a sentence of up to 20 years of prison time and/or a fine of up to $ 500,000 or twice the value of the property involved, whichever is greater. In comparison, tax evasion, as stated in 26 U.S.C. § 7201, carries a fine of not more than $ 100,000 in the case of a natural person and not more than $ 500,000 in the case of a corporation. The maximum prison time is five years. Money laundering thus carries a far longer potential prison sentence than tax evasion. The sentencing is governed by the U.S. Sentencing Guidelines (USSG). After complex factors have been applied, the Sentencing Table[70] provides a certain range that can be increased based on certain other factors. Ranges are increased in cases of "business of laundering funds" (by four levels), § 2S1.1 (2) (C), or if there is a case of "sophisticated laundering"[71] (by two levels), § 2S1.1 (b) (3). The Guideline Manuals[72] contain a commentary with specifications and definitions.

Under German law, money laundering can result in a prison sentence of between three months and five years. In particularly serious cases, it can range from six months to ten years. Examples of a particularly serious case are if the offender acts on a commercial basis or as a member of an organized group whose purpose is the continued commission of money laundering, § 261 (4) German Criminal Code. Convicted tax evaders can be fined or sentenced, quite similar, to a maximum of five years in prison. In a particularly serious case, the prison sentence is the same as for particularly serious cases of money laundering: between six months and ten years. Six examples of particularly serious cases are defined in § 370 (3) German Fiscal Code. They include deliberately understating taxes on a large scale, which begins at € 50,000 of understated taxes.[73]

Apart from a few legally defined grounds to increase or reduce the sentence, the final sentence is at the discretion of the judge who has to balance all, not only legally defined, grounds to mitigate or aggravate the sentence. Germany does not have fixed sentencing guidelines. However, the German Federal Court of Justice has decided that generally prison without parole shall be given where € 1,000,000 or more in taxes are evaded, unless, exceptionally, the circumstances justify a lower sentence.[74]

German law punishes both crimes equally, whereas US law attaches a far heavier criminal weight to money laundering than to tax evasion. In Germany, which has no guideline manuals for sentencing, the sentence is at the judge's discretion. The US Guidelines Manuals result in more even-handed sentencing in the US, and are in practice very important. Usually the sentencing considerations in the indictment and/or plea agreement are read first and then reviewed under the applicable guidelines. The calculation of exposures under the guidelines and the applicable departures and grounds for variance are in many cases assessed even before the viability of the charges or the quantum of evidence. The Guidelines

[70] See https://www.ussc.gov/sites/default/files/pdf/guidelines-manual/2016/Sentencing_Table.pdf (4.4.2020).

[71] For example, the use of fictious entities or shell companies, see Commentary of the Guidelines Manual, Part S Note 5 (A).

[72] For 2018 see https://www.ussc.gov/sites/default/files/pdf/guidelines-manual/2018/GLMFull.pdf (4.4.2020).

[73] BGH, Judgment of 2.12.2008 – 1 StR 416/08 = BGHSt 53, 71; BGH, Judgment of 27.10.2015 – 1 StR 373/15 = BGHSt 61, 28.

[74] BGH, Judgment of 2.12. 2008 – 1 StR 416/08 = BGHSt 53, 71; BGH, Judgment of 7.2. 2012 – 1 StR 525/11 = wistra 2012, 236; BGH, Judgment of 22.5. 2012 – 1 StR 103/12 = wistra 2012, 350; BGH, Judgment of 26.9.2012 – 1 StR 423/12 = wistra 2013, 31.

Manuals therefore represent a major difference between US law and German law in general.

V. Conclusion

US law, as well as German law, recognizes tax evasion as a predicate offense for money laundering. To do so, it uses a 'trick': it does not name tax evasion as a predicate offense but rather sees it as fraud. Wire and mail fraud, however, are named as predicate offenses, which indirectly makes tax evasion a predicate offense as well. German law names tax evasion as a predicate offense but only in the form of tax evasion committed on a commercial basis or as a member of an organized group.

Since both jurisdictions recognize tax evasion as a predicate offense in one way or another, they both need to find answers to questions that arise from the notion that the tax evasion crime is incoherent with the scheme of proceeds derived from an offense. Money laundering is the transaction of proceeds which derive in some form from an illegal activity. An unassessed tax claim, although a benefit from the criminal act of tax evasion, does not derive from the criminal act itself, but exists independently of it. The perpetrator does not obtain anything from tax evasion but rather keeps something that was in his or her possession already.

Answers are also needed as to how to identify proceeds within the defendant's assets and how to handle funds that contain money obtained both legally and illegally.

US law describes the proceeds of tax evasion as a "retainer" and German law as "expenditures saved". Neither jurisdiction has to date found a convincing method to identify the proceeds within the defendant's assets; both pick such proceeds arbitrarily. The author suggests that – if tax evasion is a predicate offense – the proceeds would primarily occur within those funds that are moved to hide the income on which the taxes are evaded. In cases where offshore companies are used, the money moved abroad is therefore tainted in the amount of taxes remaining unassessed. If no money is moved, but taxes are simply not declared, the tainted amount is equal to that of the unassessed taxes in the bank account from where the taxes are usually paid.

The current situation with respect to commingled accounts is unsatisfactory, especially in Germany. The highest German court sees commingled accounts, by the means of accounts containing tainted and legal funds, as one item. If tainted money is deposited into a bank account, the entire balance of the account becomes tainted if the tainted money is not insignificant from an economic point of view. The federal US courts are split on this issue. The Fourth Circuit would apply the same rule as the German Federal Court of Justice, whereas the Fifth and Ninth Circuits apply a clean-funds-first-out rule. The clean funds are used first, and the tainted money remains, like coffee grounds, in the account. Once the aggregated withdrawals exceed the clean funds in the bank account, the tainted money is used. The clean-funds-first-out rule deserves support because it is aligned with basic principles of criminal law such the burden of proof and the "beyond a reasonable doubt" standard.

When it comes to the norms themselves, the US laws are more broadly defined (for example in their use of the term "proceeds"), and the US money laundering statute allows longer prison times than the German provisions. These differences stem from the divergent approaches to the role of a prosecutor in the two jurisdictions. US law acknowledges great prosecutorial discretion in deciding whether, and to what extent, to invoke charges.[75] In practice, money laundering is often charged on top of a predicate offense and other crimes such as obstruction of justice or false statements. It is common to "pile on", or over-charge, the defendant to reach a plea bargain. Given that money laundering guidelines are harsh and white-collar cases are often lengthy and difficult to present to a grand jury, US prosecutors often avoid money laundering in an attempt to resolve short of trial eventually. Instead, they bring conspiracy, mail or wire fraud, obstruction of justice, or False Statement Act charges. Bringing simpler cases raises the likelihood of prevailing before court.[76]

In comparison, prosecutors in Germany are legally obligated to file charges and have – with a few exceptions[77] – no discretion (this is known as the 'legality principle' or Legalitätsprinzip), § 152 (2) German Code of Criminal Procedure (StPO). On one hand, this allows charges to be dropped when they are not reasonable under the given circumstances. But on the other hand, it is also an invitation for pressure and one reason for a system dominated by plea bargains.

To conclude, it is to be hoped that Germany starts a discussion on applying a clean-funds-first-out rule, or at least finds a similar approach to those currently discussed in the US.

[75] *Weaver/Burkoff/Hancock/Hoeffel/Singer/Friedland*, Principles of Criminal Procedure, 5th ed. 2016, p. 341, 344 et seq.
[76] See *Podgor/Henning/Israel/King* (fn. 48), § 1.6.
[77] For example, an investigation may be ceased if merely a minor offense occurred or ceased combined with an imposed fine, §§ 153 et seq. StPO.