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## Tax Evasion as Crime

Stuart P. Green\*

From the perspective of the criminal law, tax evasion is a baffling and anomalous offense. It deviates from the traditional paradigm of crime in that the harms it causes are highly diffuse, significant only in the aggregate, and hard to identify with any certainty. It is also one of only a handful of crimes (at least under U.S. law) that requires evidence of “willfulness” -- understood to mean a “voluntary, intentional violation of a known legal duty.”<sup>1</sup> Such culpability is quite unusual in criminal law in that it allows mistake or ignorance of the law to be a defense.

Tax evasion also differs from other offenses in terms of its incidence, which is probably higher than that of any other serious white collar crime. According to one recent study, approximately 25 percent of U.S. taxpayers admitted to deliberately cheating on their taxes.<sup>2</sup> And the level of noncompliance is even higher outside the U.S. -- in Europe, and especially in the developing world.<sup>3</sup> There are many reasons for such noncompliance, but one is certainly the fact

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<sup>1</sup> I.R.C. § 7201, interpreted in *United States v. Pomponio*, 429 U.S. 10, 12 (1976) ; see also Mark C. Winings, “Ignorance is Bliss, Especially for the Tax Evader,” *J. Crim. L. & Criminology* 84: 575 (1993) (discussing the problems with allowing an ignorance of law defense for tax crimes).

<sup>2</sup> James A. Tackett et al., “A Criminological Perspective of Tax Evasion,” *Tax Notes* 110: 654, 654 (Feb. 6, 2006), available in *Tax Notes Today*, 2006 LEXIS TNT 25-73.

<sup>3</sup> See James Alm & Benno Torgler, “Culture Differences and Tax Morale in the United States and Europe” (2006) *Journal of Economic Psychology* 27: 224; John Hasseldine & Zhuhong Li, “More Tax Evasion Research in New Millennium” (1999) *Crime, Law & Social Change* 31: 91, 91.

that a significant percentage of people believe that cheating on their taxes is not morally wrong.<sup>4</sup> And it is striking as well that there is a long and fairly respectable tradition of tax resistance as a form of political protest, something that is hard to imagine in the case of crimes such as bribery, perjury, or fraud.<sup>5</sup>

The laws concerning tax evasion are also *enforced* in a highly irregular manner (again, focusing particularly on the U.S. context). For example, in 2009, the U.S. government authorized the prosecution of only 1,210 criminal tax cases – representing a mere .00086% of the 179.4 million individual tax returns filed in that year.<sup>6</sup> And, where prosecutions do occur, they are often brought in an uneven and highly selective manner.<sup>7</sup>

Despite, or perhaps because of, such anomalies, tax evasion is a crime that has tended to fall between the cracks of normative analysis. Criminal law theorists have largely avoided the

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<sup>4</sup> See generally Leandra Lederman, “The Interplay Between Norms and Enforcement in Tax Compliance” (2003), *Ohio State L.J.* 64: 1453. In a recent Taxpayer Attitude Survey conducted by the I.R.S. Oversight Board, sixteen percent of taxpayers disagreed with the statement that they should cheat “not at all” on their taxes. Eight percent said it was acceptable to cheat “a little here and there,” and five percent said that people could cheat “as much as possible.” See IRS Oversight Board, Taxpayer Attitude Survey 2007 (Feb. 2008), [http://www.treas.gov/irsob/reports/2008/2007\\_Taxpayer-Attitude-Survey.pdf](http://www.treas.gov/irsob/reports/2008/2007_Taxpayer-Attitude-Survey.pdf)

For more on the complex psychology that underlies tax evasion, see Eric Kirchler, *The Economic Psychology of Tax Behaviour* (Cambridge University Press, 2007).

<sup>5</sup> See generally David F. Burg, *A World History of Tax Rebellions* (Routledge, 2004); Romain D. Huret, *American Tax Resisters* (Harvard University Press, 2014).

<sup>6</sup> Tax Division, U.S. Department of Justice, FY 2011 Congressional Budget 25 (2010), available at <http://www.justice.gov/jmd/2011justification/pdf/fy11-tax-justification.pdf>. See *Individual Complete Report (Publication 1304), Table 1.6, SOI Tax Stats—Individual Statistical Tables by Size of Adjusted Gross Income*, IRS, <http://www.irs.gov/taxstats/indtaxstats/>. See also Joshua D. Blank, “In Defense of Individual Tax Privacy,” *Emory L.J.* 61: 265 (2011); Bruce Hochman and Steven Toscher, “More Than Bad Luck: Differences in Civil and Criminal Fraud Sanctions under the Internal Revenue Code,” *taxlitigator.com* (2007), <http://taxlitigator.com/more-than-bad-luck-differences-in-civil-and-criminal-fraud-sanctions-under-the-internal-revenue-code/>

<sup>7</sup> There are disparities both geographically and according to the type and wealth of the taxpayer. See David Cay Johnston, “Audits Spread Unevenly Across U.S.,” *N.Y. Times* (Apr. 12, 1998), available at <http://query.nytimes.com/gst/fullpage.html?res=9E0CE4D7133DF931A25757C0A96E958260&sec=&spon=&page=wanted=print>; see also Transactional Records Access Clearinghouse, District Enforcement, *tracirs* (2010), <http://trac.syr.edu/tracirs/findings/07/index.html>; Michael Levi, “Serious tax fraud and noncompliance: a review of evidence on the differential impact of criminal and noncriminal proceedings,” *Criminology & Public Policy* 9: 493 (2010).

subject altogether (perhaps because of tax law's reputation for being highly technical).

Meanwhile, tax law theorists, though not avoiding the subject of tax evasion as such, have only rarely applied to it the basic tools of criminal law theory.

As a criminal law theorist myself, I am something of an exception here, having written about tax evasion twice before. On one occasion, I offered some preliminary thoughts on why it is wrong, from a moral perspective, to evade taxes.<sup>8</sup> On another occasion, I looked at what exactly is wrong with the *crime* of tax evasion: I considered why the rate of tax evasion is so high, why there is so much apparent skepticism about the wrongfulness of evading taxes, and why the enforcement of our laws against tax evasion is so irregular.<sup>9</sup>

In this chapter, I intend to take my analysis of tax evasion a bit further. First, I will argue that an understanding of how taxes differ from fees, fines, penalties, forfeitures, and other types of government assessments is crucial to an understanding of why tax evasion is morally wrong. Second, I will offer a more fully developed account of the moral content of tax evasion, explaining the role that the concepts of cheating, disobedience to the law, and what I call “deceptive covering up” play in defining its moral content; and why, further, the concept of stealing is largely inapposite. Finally, I will consider the extent to which my analysis of tax evasion might be helpful in assessing the moral content of tax avoidance.

## **A. Defining Key Concepts**

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<sup>8</sup> Stuart P. Green, *Lying, Cheating, and Stealing: A Moral Theory of White Collar Crime* (Oxford University Press, 2006), at 243-48.

<sup>9</sup> Stuart P. Green, “What is Wrong with Tax Evasion?,” *Houston Business and Tax Law Journal* (2009) 9: 221-36.

Before we can begin the normative analysis, it will be helpful to develop a definition of two key terms: *tax* and *tax evasion*. The account here is intended to reflect widespread, if not universal, usage, while at the same time extending the definitional analysis beyond where it has gone before.

## 1. What is a tax?

Although the “what is a tax?” question has generated a good deal of litigation and court decisions, it seems to have attracted relatively little attention from theorists.<sup>10</sup> In the U.S., the question arises primarily in the following contexts:

- Under the U.S. Constitution, measures that constitute “taxes” must originate in the House of Representatives, must be imposed “uniformly” throughout the United States, may be used only “to pay the Debts and provide for the common Defence and general Welfare of the United States,” may not be levied on exports, and may not be imposed as a condition of the right to vote.<sup>11</sup> Other kinds of government fees lack such limitations. Similarly, many state constitutions require that tax legislation be enacted by a larger legislative majority than normal, or that they be passed by referendum. Thus, in order to determine if constitutional requirements have been complied with, courts at both the federal and state level have had to decide which

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<sup>10</sup> Worth noting here is Bruno Peeters et al. (eds) *The Concept of Tax* (European Association of Tax Law Professors Congress, 2005), [http://www.eatlp.org/uploads/public/part I concept of tax in eu member states 05\\_05\\_09.pdf](http://www.eatlp.org/uploads/public/part_I_concept_of_tax_in_eu_member_states_05_05_09.pdf)

<sup>11</sup> See generally Steve R. Johnson, “Obamacare and the ‘What is a Tax?’ Question,” *State Tax Notes* (Jan. 9, 2012), at 155; Robert G. Natelson, “What the Constitution Means by ‘Duties, Imposts, and Excises’ – and ‘Taxes’ (Direct or Otherwise),” *Case Western Reserve. L. Rev.* vol. 66 (forthcoming, 2016), available on SSRN (March 2, 2015), [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2572633..](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2572633..)

assessments are properly understood as taxes and which constitute some other kind of assessment.<sup>12</sup>

- The federal and state constitutions also impose separate procedural requirements on other kinds of (non-tax) government assessment. For example, if a government assessment is determined to be a “criminal fine,” it must comply with a defendant’s right: to confrontation, against double jeopardy, against self-incrimination, and to have his guilt decided beyond a reasonable doubt.<sup>13</sup> Similarly, if a government assessment is determined to be a “taking,” it will be prohibited under the Constitution’s Takings Clause unless the government offers the property owner just compensation.<sup>14</sup> Courts have thus had to distinguish between measures that are really taxes and those that are in fact criminal fines or takings, as the case may be.

- The question of “what is a tax?” also arises in a host of statutory contexts. For example, under the Internal Revenue Code itself, a taxpayer who paid foreign “taxes” to a foreign country on foreign source income and is subject to U.S. tax on the same income is often entitled to a credit or itemized deduction for those taxes.<sup>15</sup> Similarly, under U.S. bankruptcy law, the claims

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<sup>12</sup> See, e.g., *Sinclair Paint Co. v. State Board of Equalization*, 15 Cal. 4th 866 (1997) (upholding as a “fee,” rather than a tax, a California provision imposing a charge on persons selling products that contain lead).

<sup>13</sup> On taxes vs. criminal fines, see, e.g., *Department of Revenue v. Kurth Ranch*, 511 U.S. 767 (1994) (invalidating Montana’s so-called Dangerous Drug Tax, which imposed fees “on the possession and storage of dangerous drugs,” on the grounds that it was really a form of punishment and therefore required various procedural protections).

<sup>14</sup> On taxes vs. takings, see Johnson, above, at 157 (pointing out that, if the government had to compensate citizens for money taken through revenue-raising tax measures, such measures would be self-defeating).

<sup>15</sup> See Treas. Reg. § 1.901-2(a)(2)(i) (2008) (payment made abroad is a “tax” if it constitutes a “compulsory payment pursuant to the authority of a foreign country to levy taxes”); see also See Internal Revenue Service, “What Foreign Taxes Qualify For The Foreign Tax Credit?” (updated, December 13, 2014), <http://www.irs.gov/Individuals/International-Taxpayers/What-Foreign-Taxes-Qualify-For-The-Foreign-Tax-Credit%3F>

of states for excise taxes owed by debtors have priority status and are non-dischargeable, but that treatment does not apply to measures that are called taxes but are determined in fact to be fines.<sup>16</sup>

Unfortunately, the cases that address the “what is a tax?” issue tend to take an ad hoc approach, offering no clear, comprehensive definition or overarching set of criteria for distinguishing taxes from other kinds of payments to the government – whether they be “user fees,” “criminal fines,” “forfeitures,” “takings,” “civil penalties,” or other “regulatory measures.” It is therefore worth trying to derive a more general definition of what should be regarded as a tax.

As a preliminary matter, I would suggest that the concept be defined as: (1) an exaction of money; (2) imposed and collected by a government authority; (3) on or from a private person or entity; where (4) such payment is compulsory; (5) imposed for non-punitive purposes; and (6) paid not in return for a specific service or privilege received from the government, but rather as a means to fund government operations more generally.<sup>17</sup>

Let us consider each element in turn: First, a tax involves the payment of money. Normally, taxes are assessed as a percentage of: the amount of money earned or received in some transaction (as in the case of income, gift, and inheritance taxes), the value of property owned (as in the case of real estate taxes), or the amount of money spent (as in the case of sales, excise, and ad valorem taxes). Some taxes are also assessed on a flat, per capita or per family unit (as in the case of poll and head taxes). When a taxpayer pays a tax, it is his choice which assets to liquidate or deplete in order to defray liability.<sup>18</sup> This is in contrast to government

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<sup>16</sup> See 11 U.S.C. § 507(a)(8)E(ii).

<sup>17</sup> For a similar, though slightly simpler, definition, see M. Barassi, “The Notion of Tax and the Different Types of Taxes,” in Peeters, *The Concept of Tax*, above, at 33.

<sup>18</sup> Johnson, above, at 158.

takings and forfeitures, which are directed at a particular asset or group of assets (such as a house, a car, or stocks and bonds.). Other kinds of compulsory, non-punitive obligations should also avoid categorization as taxes. For example, conscription in the military would not be a tax, even if the conscript incurred opportunity costs, including loss of income, while fulfilling his service obligation.

Second, the requirement of payment must be imposed by a governmental entity. Thus, membership fees paid to a private organization would not qualify as a tax. Nor would payments to a political candidate, political party, or individual government official (whether legal or not). The government entities that assess taxes are typically legislative bodies, while the collection of taxes is normally performed by an administrative body (though this last feature seems to be a contingent rather than necessary condition of a tax scheme).

Third, the obligation to pay must be imposed on members of a class of private persons or entities. This means that a “transfer” or “forgiveness” payment made by one government entity to another -- say, within a federal system -- would not count as a tax. Nor would payments required of a particular individual only (as in the case of a forfeiture).

Fourth, the payment must be compulsory. Money given voluntarily to the government for the benefit of the public -- say, to create a public park or refurbish a public museum -- would not constitute a tax. Nor would (admittedly rare and, somewhat paradoxically, tax-deductible) gifts made to the U.S. Department of Treasury’s Bureau of Public Debt for the purpose of paying down the debt.<sup>19</sup> Also not qualifying as a tax would be money paid for the purchase of Treasury

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<sup>19</sup> Approximately 1.8 million dollars in gifts were given to the U.S. Treasury during 2013. Gregory Korte, “As National Debt Soars, Gifts to Pay it off Decline,” *USA Today* (Dec. 20, 2013), <http://www.usatoday.com/story/news/politics/2013/12/19/gifts-to-reduce-the-public-debt-decline/4059787/>

or municipal bonds, even if the proceeds of such bond offerings were used to fund public services.

Fifth, the payment must be non-punitive. Therefore, money paid or property forfeited to a government as a fine or penalty imposed in response to a citizen's law breaking would not qualify as a tax, even if such money or property was used for general purposes. One question here is whether the assessment imposed for late payment of a tax should itself be regarded as a tax, or whether instead it should be thought of as a penalty. I would say that that part of the assessment meant to punish and deter late payment should properly be understood as a penalty or fine, rather than as a tax. On the other hand, to the extent that such penalty includes an interest payment meant to compensate the government for the present value of tax revenue lost, it could reasonably be characterized as part of the tax itself.

Finally, and most complexly, to be a tax, a payment must be made not in return for a specific good or service or other economic benefit provided by the government to an individual or group of individuals, but rather for general purposes. Thus, money paid as tuition for attendance at a public university and tolls paid for the privilege of using a public bridge or tunnel should not be regarded as taxes. Both of these payments are properly viewed as fees which, in contrast to a tax, involve the payment of money for a particular good, service, or benefit not automatically conferred upon the general public. Payment of a fee can be avoided if one chooses not to take advantage of the benefit offered.<sup>20</sup> To say that fees are paid for a particular service, however, is not to suggest that tax revenues must always go into a general fund. For example, a sales tax on cigarettes the proceeds of which were used exclusively to support public schools or

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<sup>20</sup> See *Executive Aircraft Consulting, Inc. v. City of Newton*, 252 Kan. 421, 427 (1993), quoted in *Johnson*, at 158.

health clinics would still be a tax, so long as the tax liability was not directly tied to the taxpayer's receipt of services.

In practice, of course, the distinction between taxes and other kinds of government exactions is not always clear. For example, under the Federal Insurance Contributions Act (known as FICA), U.S. wage earners are required to make payments which are used to support the federal Social Security and Medicare programs. The amount one pays in FICA taxes throughout one's working career is partly, though not completely, correlated with the amount one is entitled to receive after one retires. The more one pays in, the more one is supposed to get back. It would therefore seem that FICA is a tax only in part, because it also functions as a government-funded annuity program.<sup>21</sup>

Similarly, "benefit taxes," such as those on motor fuels, are tied to the costs of providing public services, such as public roads. They also reflect a dual character: On the one hand, the heavier one's use of public roads, the more fuel one will likely have to buy, and the more money one will owe in gasoline tax. In that sense, gasoline taxes function as a fee: payment is correlated to use of government goods or services. On the other hand, the correlation is a loose one: a person can use streets and highways without paying gasoline tax (say, if she rides a bicycle or drives an electric car), and she can buy fuel without making use of the roads (say, if the fuel is being used in a tractor driven on her privately owned farm).

Given all of these complexities in trying to define the concept of "tax," one might be tempted to take a different approach. Rather than thinking of "tax" as a bright line category into which a given government exaction either falls or does not fall, we might think of it instead as a

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<sup>21</sup> Cf. Kevin A. Hassett, "Is the Payroll Tax a Tax?" *National Review Online* (March 29, 2005), <http://www.nationalreview.com/article/214027/payroll-tax-tax-kevin-hassett?target=author&tid=900912> (arguing that reduction in social security benefits is equivalent to increase in tax).

quality that a given exaction might reflect to one degree or another.<sup>22</sup> Under this approach, rather than saying that one exaction is a tax and another is not, we should instead say that a given exaction is more or less tax-like. For example, we might say that FICA is “less tax-like” than income or sales tax because it benefits payers in a more direct manner than taxes of those sorts. While I have no objection in principle to such an approach (indeed, I follow a similar approach later in this chapter, when considering the distinction between *mala in se* and *mala prohibita*), it is worth recalling that, in practice, courts often will have to decide definitively whether or not a given exaction is a tax.

There is also another definitional issue that needs to be addressed. So far, we have been speaking of “taxes” as if they always involved an obligation of a citizen to pay money to the government. But as many tax scholars have explained, although the principal goal of the tax law is to raise revenue, taxes are also used as an economic and social policy tool. The tax code does far more than just determine what constitutes “income” to be taxed. It also decides what deductions and exemptions will be allowed, thereby encouraging supposedly socially beneficial conduct such as charitable giving, home ownership, and saving for retirement. And, these scholars argue, from an economic perspective, there is no real difference between encouraging some activity by reducing taxes owed and doing so by directly subsidizing that activity through government payments. From that perspective, as Dan Shaviro has explained, the distinction

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<sup>22</sup> See William Barker, “The Relevance of a Concept of Tax,” in Peeters, *The Concept of Tax*, at 7 (arguing that we should think of taxes as “charges on a sliding scale, which varies inversely with the degree of the private benefit and the significance of the public good”); Marc Bourgeois, “Constitutional Framework of the Different Types of Income,” in Peeters, at 100 (“there is a continuum, ranging from pure taxes where the taxpayer receives nothing, to fees for services whose value corresponds to what was previously paid by the government”).

between taxes and spending is one of “pure form.”<sup>23</sup> Indeed, this is the basic insight of “tax expenditure” analysis.<sup>24</sup>

But the fact that tax breaks and government spending have similar economic effects does not imply that the concept of “tax” must somehow include all government expenditures. The point of tax expenditure theory is not to expand the definition of tax, but rather to recognize that “certain provisions of the tax laws are not really tax provisions, but are actually government spending programs disguised in tax language.”<sup>25</sup> If anything, the insights of tax expenditure theory should lead to a contraction in the definition of what constitutes a “tax,” not an expansion.

## 2. What is tax evasion?

Having considered the meaning of *tax*, we can now consider the meaning of *tax evasion*. The concept is used in different ways in different criminal codes, and it will not be possible to find any universally applicable definition. However, I would like to consider three elements that appear in the definition of tax evasion used in many jurisdictions.

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<sup>23</sup> Daniel N. Shaviro, “Rethinking Tax Expenditures and Fiscal Language” (2004), *Tax Law Review* 57: 187, 191. See also Miranda Perry Fleischer, “Libertarianism and the Charitable Tax Subsidies,” *Boston College L. Rev.* \_\_ vol. 56 (forthcoming, 2015).

<sup>24</sup> As Stanley Surrey and Paul McDaniel put it in their seminal article:

Whenever government decides to grant monetary assistance to an activity or group, it may elect from a wide range of methods in delivering that assistance. A direct government grant or subsidy may be made; a government loan may be made, perhaps at a special interest rate; a private loan may be guaranteed by the government; and so on. In contrast, the government may use the income tax system and reduce the tax otherwise applicable, by adopting a special exclusion, deduction or the like for the favored activity or group. Examples are investment credits, special depreciation deductions, deductions for special forms of consumption, low rates of tax for certain activities, and so on. These tax reductions, in effect, represent monetary assistance provided by the government.

Stanley S. Surrey and Paul R. McDaniel, “the Tax Expenditure Concept and the Budget Reform Act of 1974,” (1976) *Boston College Industrial and Commercial Law Review* 17: 689.

<sup>25</sup> Victor Thuronyi, “Tax Expenditures: A Reassessment,” *Duke L.J.* 1988: 1155, 1155.

First is the idea of noncompliance. Tax evasion always involves a nonpayment or underpayment of taxes actually owed, whether by understating income, overstating deductions or exemptions, or simply failing to pay what is owed. Indeed, as we shall see below, the fact that a citizen has failed to pay the taxes he owes is what distinguishes tax evasion from mere tax avoidance. Both may cause similar harms and be motivated by similar motives, but only the first violates the law (assuming that tax avoidance has not been transformed into tax evasion through a taxpayer's defiance of a general anti-avoidance rule, or GAAR).<sup>26</sup>

Second is the mental element. There is no tax evasion if *T*'s failure to pay taxes was inadvertent. In many jurisdictions, tax evasion requires not only an intent not to pay, but also actual knowledge of the legal duty owed. Tax evasion thus differs from most other crimes, which are governed by the rule of *ignorantia legis neminem excusat*.<sup>27</sup>

A third element appears in some tax evasion statutes, though it is less widely observed and seems less central from a conceptual standpoint. In at least a few countries (including the U.S., Switzerland, the Philippines, and perhaps Nigeria), the crime of tax evasion requires not only that the evader purposefully avoid paying taxes owed, but also that he also take affirmative steps to avoid detection – say, by keeping a second set of books or fabricating records.<sup>28</sup> In the

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<sup>26</sup> In many jurisdictions, tax authorities have the power, through GAARs, to deny taxpayers the benefit of an arrangement that they have entered into for an impermissible purpose. Where a taxpayer has engaged in such prohibited practice, and persists in claiming the tax benefit, it makes sense to say that *at that point* he is committing tax evasion.

<sup>27</sup> “Ignorance of the law is no excuse.” See *Cheek v. United States*, 498 U.S. 192 (1991).

<sup>28</sup> Under U.S. law, willful nonpayment of taxes simpliciter (including the failure to file a return) is generally treated as a misdemeanor offense under I.R.C. § 7203. Such noncompliance is contrasted to tax “evasion” proper, which carries a penalty of five years in prison under § 7201, and requires not only the willful nonpayment of taxes but also some additional concealment of one’s activities. In Switzerland, failing to pay taxes and covering it up is known as “tax fraud.” See Swiss Federal Law on Direct Federal Tax (article 186) and the Federal Law on Harmonising the Direct Taxation of Cantons and Municipalities (article 59), described in Staiger, Schwald & Partner, “Tax Fraud and Tax Evasion,”

[http://www.geneve-finance.ch/sites/default/files/pdf/Topic\\_4\\_Tax\\_fraud\\_and\\_tax\\_evasion.pdf?contentid=2409](http://www.geneve-finance.ch/sites/default/files/pdf/Topic_4_Tax_fraud_and_tax_evasion.pdf?contentid=2409)

U.S. context, at least, this distinction – between underpayment *simpliciter* and underpayment plus covering up – marks the line between nonpayment of taxes as a misdemeanor or civil wrong and nonpayment of taxes as a serious felony offense. As we will see below, this final element, when present, adds something significant to tax evasion’s moral content.

Finally, as we saw above, under the tax expenditure approach, there is an argument that taxes, broadly defined, should be understood to include not just payments by citizens to the government, but also payments by the government to citizens. If this were right, it would raise the question whether one can evade taxes not just by failing to pay taxes due but also by unlawfully claiming government entitlements above and beyond tax due, as under an earned income tax credit scheme. For reasons I’ll explain below, I believe this would be a mistake. Simply because two transactions are economically equivalent does not necessarily mean that they are morally or legally equivalent.

## **B. The Moral Content of Tax Evasion**

Under the hybrid theory of punishment that I have endorsed and articulated on previous occasions, moral blameworthiness is a necessary (though not sufficient) condition for an act’s being justly subject to criminal punishment.<sup>29</sup> Thus, if we want to know whether and why tax evasion should be a crime, we would need to know the various ways in which it is morally blameworthy. One key element of any blameworthiness analysis is wrongfulness. As I have

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In the Philippines, tax evasion can involve use of fictitious receipts, the keeping of double sets of books, false or fictitious entries in books, fictitious transactions in the name of dummy corporations, and the like. See Rosario G. Manason, “Tax Evasion in the Philippines,” (1988) *J. Philippine Development* 15: 167, <http://dirp3.pids.gov.ph/ris/pjd/pidsjpd88-2tax.pdf>

For a discussion of what constitutes tax evasion in Nigeria, see Teju Somorin, “Tax Evasion in Africa: Kinds of Evasion, How to Control it – The Nigerian Experience” (2010), <http://unpan1.un.org/intradoc/groups/public/documents/cafrad/unpan043343.pdf>

<sup>29</sup> Green, *Lying, Cheating, and Stealing*, above, at 30-47.

explained elsewhere, “moral wrongfulness” reflects the extent to which a criminal act involves the violation of a freestanding moral norm, rule, right, or duty.<sup>30</sup> (This is in contrast to “harmfulness,” which reflects the degree to which a criminal act causes, or risks causing, what Joel Feinberg called a “significant setback to another’s interests.”<sup>31</sup>) Elsewhere, I have taken a preliminary look at the various ways in which tax evasion might be understood as wrongful.<sup>32</sup> Here, I want to modify, expand on, and correct some of that earlier analysis.

There are three alternative paradigms under which the moral wrong in tax evasion has traditionally been conceptualized: (1) as a form of “stealing,” (2) as a form of “cheating,” and (3) as a violation of the “moral obligation to obey the law.” In what follows, I shall argue that while the concept of stealing proves, on inspection, to be mostly inapposite, cheating and disobedience to the law, as well as deceptive “covering up,” are all key to understanding why tax evasion is morally wrongful.

## **1. Tax evasion as stealing**

Tax evasion has often been spoken of as a form of “stealing.”<sup>33</sup> This view is problematic. In other work, I described the complex legal, moral, psychological, and cultural meanings that characterize the act of stealing and the crime of theft.<sup>34</sup> Stealing has traditionally involved a particularly substantial interference with an owner’s property rights, including, often, the right of

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<sup>30</sup> See *id.*

<sup>31</sup> Joel Feinberg, *Harm to Others* (Oxford University Press, 1984), *passim*.

<sup>32</sup> Green, *Lying, Cheating, and Stealing*, above, at 243-48.

<sup>33</sup> See, e.g., Martin T. Crowe, *The Moral Obligation of Paying Just Taxes* 42 (Catholic University of America, Studies in Sacred Theology #84, 1944).

<sup>34</sup> Stuart P. Green, *Thirteen Ways to Steal a Bicycle: Theft Law in the Information Age* (Harvard University Press, 2012), 91-114.

possession. It involves not just a temporary violation of the owner's right to exclude others from using the property, but also a more permanent violation of the owner's right to use it himself.

Stealing, crucially, involves an involuntary transfer of property from victim/owner to thief. This transfer can be considered in terms of a common sense (if not strict economic) notion of zero sum-ness: what is the thief's gain must be the victim's loss.<sup>35</sup> Stealing thus represents a particularly significant assault on one's "endowment." (As behavioral economists have explained, people ascribe more value to things they have in their possession, *ceteris paribus*, than they do to things owned by someone else.<sup>36</sup>)

Evasion of taxes, as properly understood, fails to satisfy this stealing paradigm. To see why, contrast two cases, the first involving stealing, but no tax; the second involving a tax, but no stealing. In the first case, homeowner *A* receives an assessment from his local municipality for the town-supplied water he uses. *A* could legally avoid paying the assessment by simply not using the town's water, and, say, using bottled water instead. But if *A* did in fact use the water, and then failed to pay the assessment, he would be depriving the municipality of a specific good without paying for it.<sup>37</sup> The zero sum paradigm would be satisfied; he would be committing theft.<sup>38</sup> He would not, however, have committed tax evasion, since the assessment that *A* failed

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<sup>35</sup> *Id.* at 210-11.

<sup>36</sup> The *locus classicus* is Daniel Kahneman and Amos Tversky, "Choices, Values, and Frames," *American Psychology* 39: 341 (1984); see also Maynard Smith, *Evolution and the Theory of Games* (Cambridge University Press, 1992).

<sup>37</sup> Unfortunately, this is more than a law professor's hypothetical. Theft of water from municipal authorities has become an increasingly serious problem in the wake of recent drought conditions in California. See "Water Thefts on Rise in Drought-Stricken California," *New York Times* (Feb. 23, 2105), <http://www.nytimes.com/aponline/2015/02/23/us/ap-us-california-drought-water-thefts.html>

<sup>38</sup> I have intentionally used a hypothetical involving an assessment for a "tangible good" like water rather than for a "public good" such as a road or bridge, because the zero-sumness of such public good use is somewhat more complicated than in the case of tangible goods. The problem is that public services are, in economic terms, excludable, but not rivalrous. They are excludable because nonpaying consumers can ordinarily be excluded from

to pay is not properly understood as a tax; rather, it's a fee. Moreover, we would normally expect the proceeds from the water assessment to be used specifically for system maintenance, rather than for general governmental purposes, though the use of the funds is not the decisive factor. The key point is that the fee charged is directly correlated with the good received.

The case in which *A* failed to pay his water bill can be contrasted to a second case in which homeowner *B* failed to pay the assessment imposed by his local municipality based on the value of his house. Here, *B* would not be paying for any *particular* good or service. The revenues from this tax would typically be used for general purposes: to support the public schools, the police, sanitation department, and other public works. And *B* would owe the same payment regardless of whether he actually made use of any of these services (for example, he may choose to send his children to private school or to employ private security or sanitation services). Here, the zero sum paradigm would *not* be met. This would not be theft; rather, it would be tax evasion.

A person who intentionally failed to pay sales tax or VAT would also be committing tax evasion. While it is true that such taxes are tied directly to the *purchase* of goods, they are not tied to the *receipt* by the taxpayer of any particular benefit from the government. The tax is tied to the purchase of goods only as a means for determining the amount of tax owed, just as income tax is determined on the basis of income earned. In none of these cases would *B* have committed theft; rather, he would have failed to pay a debt that is owed. In such cases, we should say not that *B* was a thief, but rather that he was a debtor in default.

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use, but they are not necessarily rivalrous because the use of a bridge or road by *D* does not preclude simultaneous use by others, at least as long as there is no overcrowding. My point is simply that while *A*'s knowing use of water without payment constitutes a clear case of theft under the zero sum paradigm, his knowing use of a public bridge or road presents a more complicated case.

Consider other cases in which *B* fails to pay a debt he owes to *C*. For example, he might breach a contract, fail to pay child support, default on his mortgage, or fail to pay a tort judgment entered against him. In none of these cases would we normally say that *B* had stolen.<sup>39</sup> *B* would not have dispossessed another of property, and the zero sum paradigm would not be satisfied. Such cases can be distinguished from ones in which *B* takes money from *C*'s wallet or bank account without his consent. Although the economic impact on *C* would be the same, from a moral (and legal) perspective, the cases would be distinguishable. Only in the second kind of case would we say that *B* has stolen from *C*.

This is not to say that one could never steal *in connection with* a tax scheme. Recall the discussion above concerning tax expenditure theory. As we saw, the taxes people pay the government are part of a much larger and more complex system in which the government both gives tax breaks and make direct expenditures to promote various social goals. For example, under the earned income tax credit program, a working person with low income can have his taxes reduced, and in some cases may even receive a payment for an amount greater than that of any tax otherwise owed – meaning that the government essentially pays the wage earner money.<sup>40</sup> If *X* lied to the IRS about how much he earned or how much his business expenses were, and thereby avoided taxes he owed, that would be tax evasion. But if *X* lied to the IRS about his earned income tax status, and thereby obtained money *above and beyond any taxes*

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<sup>39</sup> The only exception is where *B* falsely agrees to honor the terms of a contract *at the time he entered into it* – that is, where he never intended to honor the contract in the first place; in that special case, we can say that *B* committed false pretenses or fraud, both of which are properly understood as forms of stealing. For further discussion of the differences between theft, fraud, and breach of contract, see Green, *Thirteen Ways to Steal a Bicycle*, at 87-90.

<sup>40</sup> Jonathan Barry Forman, “Earned Income Tax Credit,” *Tax Policy Center*, <http://www.taxpolicycenter.org/taxtopics/encyclopedia/EITC.cfm>

*owed*, he would on my view be committing theft or false claims.<sup>41</sup> And this distinction should hold even if the economic effect on the government would in some sense be the same in each case.

Another tax-related case in which theft is committed is where sales tax is collected by a seller from buyers at the point of purchase, and the seller then fails to turn over the proceeds, as required, to the state. Such cases *are* properly understood as theft, rather than as tax evasion. It was, after all, the buyer, not the seller, who had the obligation to pay the tax, and that obligation was discharged. The seller was simply holding the buyer's tax payment in a kind of trust, in the same way a bank or credit card company might hold money in trust for a customer. The seller who failed to turn over the sales tax proceeds would essentially be committing embezzlement.<sup>42</sup>

Yet another puzzle is raised by cases in which A pays no sales tax because he acquired a good through stealing rather than purchase. Could he be charged with evading sales tax? Sales tax typically applies to “transfer[s] of title or possession, exchange, or barter . . . *for a consideration*.”<sup>43</sup> Because thefts, by definition, involve no consideration, there is no sale, therefore no sales tax due, and therefore no evasion of sales tax. A more appropriate way to think about such cases is as an evasion of income tax, analogous to cases in which defendants are prosecuted for evading tax on income earned from the sale of drugs, from bribes, or through racketeering activities (think of Al Capone). In those cases, the tax code makes clear that income

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<sup>41</sup> This view is also supported by the language of the basic tax evasion provision, which says that a person evades taxes if he “willfully attempts in any manner to evade or defeat any tax imposed by this title or the payment thereof.” 26 U.S.C. § 7201.

<sup>42</sup> For an example of such reasoning, see *State v. Chapman Dodge Center, Inc.*, 428 So. 2d 413 (La. 1983).

<sup>43</sup> E.g. California Revenue and Taxation Code § 6606(a) (emphasis added).

tax must be paid regardless of whether income was earned legally or illegally, including through theft.<sup>44</sup>

There is one additional reason to reject the view that tax evasion should ordinarily be understood as a form of theft. In our system of law, almost all thefts are treated as crimes, even those that involve the stealing of low value items.<sup>45</sup> *Civil* theft, by contrast, is a fairly exotic cause of action.<sup>46</sup> In the case of tax evasion, the pattern is reversed: as noted above, only a tiny percentage of all cases of tax evasion are prosecuted criminally. The remainder are handled as civil violations, if at all. If tax evasion really were a species of theft, we would expect it to be treated much more consistently as a crime.<sup>47</sup>

## 2. Tax evasion as cheating

In previous work, I argued that, rather than thinking of tax evasion as a form of stealing, we would do better to think of it as a form of “cheating,” which I defined more generally as the: (1) violation of a (2) fair and (3) fairly enforced rule (4) with the intent to obtain an advantage over some party (5) with whom the rule-breaker is in a (6) cooperative, rule-governed relationship.<sup>48</sup> This account, I argued, had several advantages: It squared well with our common

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<sup>44</sup> Internal Revenue Code § 61; I.R.S. Publication 17 <http://www.irs.gov/publications/p17/ch12.html> (“other income” includes property obtained through stealing, bribes, and other illegal activities, such as selling drugs).

<sup>45</sup> See Green, *Thirteen Ways to Steal a Bicycle*, at 161-65.

<sup>46</sup> *Id.* at 137-38.

<sup>47</sup> It is also worth pointing out that just because tax-evader *A* *cheats* his fellow citizens does not mean that he also *steals* from them. In theory, it is true that if *A* fails to pay the taxes he owes, other taxpayers somewhere down the line will presumably have to pick up the slack and pay more in taxes (either that, or the government will have to reduce expenditures). But, while such behavior does constitute a form of cheating, it does not constitute stealing, since stealing requires that *A* deprive a property owner of his rights in property, and there is no indication that this has happened when *A* fails to pay his taxes.

<sup>48</sup> Green, *Lying, Cheating, and Stealing*, at 247. For another work that emphasizes the significance of cheating, see Donald Morris, *Tax Cheating: Illegal—But is it Immoral?* (State U. Press of New York, 2012).

way of speaking of tax evasion as “cheating on one’s taxes.” It reflected the fact that evading taxes causes harm not just to the government but also to one’s fellow citizens, who are forced to bear a heavier burden as a result of one’s conduct. And it pointed to parallels between the moral content of tax evasion and other white collar offenses such as insider trading, various kinds of fraud, and various regulatory crimes.<sup>49</sup>

It should be clear, however, that not all rule violations entail cheating. Consider a case in which a driver drives through a red light at 3:00 a.m. on a deserted rural road. The driver has violated the rule that requires drivers to stop at red lights, but he has not, in all likelihood, achieved an unfair advantage over anyone, and he has therefore not cheated. (This might not be true of every traffic offense: one can imagine a case in which a driver violates the rules of the road by, say, driving on the soft shoulder in order to get ahead of other drivers in a traffic jam. That would, on my account, be a form of cheating.)

Tax evasion, in contrast to the red light case, does potentially involve cheating: The tax evader violates the rule that requires citizens to pay the specific taxes they owe, and he normally does so for the purpose of obtaining an advantage over others. The tax evader is a free rider: he fails to pay his fair share of keeping our government running, while continuing to reap, or potentially reap, the benefits of being a citizen.

The point I am making about the centrality of cheating to our understanding of tax evasion bears some similarity to a point made by Herbert Morris, who argued that:

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<sup>49</sup> Caron Beaton-Wells has also found the concept of cheating helpful in understanding the criminalization of price fixing. See “Capturing the Criminality of Hard Core Cartels: The Australian Proposal,” *Melbourne University Law Review* 31: 675 (2007).

[I]t is just to punish those who have violated the rules and caused the unfair distribution of benefits and burdens. A person who violates the rules has something others have -- the benefits of the system -- but by renouncing what others have assumed, the burdens of self-restraint, he has acquired an unfair advantage. Matters are not even until this advantage is in some way erased. Another way of putting it is that he owes something to others, for he has something that does not rightfully belong to him. Justice -- that is punishing such individuals -- restores the equilibrium of benefits and burdens by taking from the individual what he owes, that is, exacting the debt.<sup>50</sup>

Although he does not use the term, Morris does a good job of explaining the basic dynamic of what is, in essence, cheating: In violating a rule that others follow, and thereby breaching an obligation to restrict his liberty in a manner agreed, the cheater gains an unfair advantage.

A problem with Morris's theory, however, is that it puts more weight on the concept of cheating than it is capable of supporting. Morris was wrong to suggest that the idea of cheating underlies *all* crimes. As Jean Hampton explained, Morris's approach "makes sense only if we believe that constraining ourselves so that we do not rape or murder or steal imposes a cost upon us. Yet that idea makes sense only if [we accept the absurd notion that] raping, murdering, and stealing are viewed by us as desirable and attractive."<sup>51</sup>

Yet, while the idea that one's acts have created an "unfair distribution of benefits and burdens" is insufficient to explain offenses like rape and murder, it can play a significant role in defining offenses such as tax evasion, since non-payment of taxes is a something that many

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<sup>50</sup> Herbert Morris, "Persons and Punishment" (1968), *The Monist* 52: 475. The argument in this and succeeding paragraphs is borrowed from Green, *Lying, Cheating, and Stealing*, at 55-56.

<sup>51</sup> Jean Hampton, "Correcting Harms Versus Righting Wrongs: The Goal of Retribution," *UCLA L. Rev.* (1992) 39: 1659, 1660.

people would find desirable and attractive, and since it does tend to create an unfair distribution of benefits and burdens.

### **3. Is there tax evasion that does not constitute cheating?**

Under the account referred to above, A should properly be understood to have cheated if and only if (1) the rule that he violates is fair and enforced in an evenhanded manner, and (2) he intends to obtain an unfair advantage over others. This would suggest that citizens who fail to pay taxes that are not fair, or who do not intend to obtain an advantage over others, have not cheated.

Both possibilities need to be considered. Looking again at U.S. law, we see a tax system that is less progressive than the tax systems of most other industrialized nations, and much less so than it was for most of the 20th century. The top marginal rate in the U.S. is now only 39.6 percent, compared to a rate of 94 percent during World War II and about 70 percent through the 1960s and 1970s. And the effective tax rate that many of the wealthiest individuals pay is actually considerably lower than 39.6 percent.<sup>52</sup> Moreover, the U.S. tax code contains countless provisions seemingly enacted for no reason other than to benefit special interest groups that have typically given large contributions to political candidates.<sup>53</sup> The code is also so complex that

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<sup>52</sup> According to economist Joseph Stiglitz, the richest 400 individual taxpayers in the U.S., with an average income of more than \$200 million, pay less than 20 percent of their income in taxes — far lower than mere millionaires, who pay about 25 percent of their income in taxes, and about the same as those earning a mere \$200,000 to \$500,000. And in 2009, 116 of the top 400 earners — almost a third — paid less than 15 percent of their income in taxes. Joseph E. Stiglitz, “A Tax System Stacked Against the 99 Percent,” *New York Times* (April 14, 2013), [http://opinionator.blogs.nytimes.com/2013/04/14/a-tax-system-stacked-against-the-99-percent/?\\_r=0](http://opinionator.blogs.nytimes.com/2013/04/14/a-tax-system-stacked-against-the-99-percent/?_r=0); see also Kim Parker, “Yes, the Rich Are Different,” *Pewsocialtrends.org* (2012), <http://www.pewsocialtrends.org/2012/08/27/yes-the-rich-are-different/>

<sup>53</sup> These arguably include tax breaks for owners of vacation homes, racetracks, beer breweries, oil refineries, hedge funds, and movie studios, to name just a few beneficiaries of presumably unfair tax laws. See generally Stiglitz, *id.*; David Cay Johnston, *Perfectly Legal: The Covert Campaign to Rig our Tax System to Benefit the Super Rich—and Cheat Everyone Else* (Portfolio, 2003); Citizens for Tax Justice, “The Sorry State of Corporate Taxes: What Fortune

only the wealthy can afford the tax advice needed to take full advantage of the many devices it offers for lowering one's tax burden lawfully.<sup>54</sup> It is no surprise that a majority of Americans now say that the income tax system is unfair.<sup>55</sup>

The tax laws are also *enforced* in a manner that is arguably unfair (again, focusing on the U.S. experience). As noted above, in 2007, the I.R.S. examined less than one percent of the approximately 179.4 million returns filed.<sup>56</sup> And the thoroughness of these audits has been dropping as well. According to the Independent Transactional Records Clearinghouse, the typical amount of time auditors spend on large corporate audits has decreased by twenty percent in recent years.<sup>57</sup> There are also large disparities from district to district, with residents in the New York metropolitan area, for example, being subject to relatively low rates of audits and prosecution, and residents of California subject to much higher rates.<sup>58</sup>

Whether a given tax regime really is so unfair that people who evade it should not be regarded as cheating is, of course, an immensely difficult question, requiring both a sophisticated

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500 Firms Pay (or Don't Pay) in the USA And What they Pay Abroad — 2008 to 2012" (February 2014), <http://www.ctj.org/corporatetaxdodgers/sorrystateofcorptaxes.pdf>

<sup>54</sup> These include deferring compensation, changing the timing of capital income to convert short term gains into long term gains, and converting ordinary income or losses to capital gains or losses. See U.S. Senate Committee on Finance, "How Tax Pros Make the Code Less Fair and Efficient: Several New Strategies and Solutions" (March 3, 2015), [http://www.finance.senate.gov/imo/media/doc/030215%20How%20Tax%20Pros%20Make%20the%20Code%20Less%20Fair%20and%20Efficient%20-%20Several%20New%20Strategies%20and%20Solutions\\_FINAL%20cover.pdf](http://www.finance.senate.gov/imo/media/doc/030215%20How%20Tax%20Pros%20Make%20the%20Code%20Less%20Fair%20and%20Efficient%20-%20Several%20New%20Strategies%20and%20Solutions_FINAL%20cover.pdf)

<sup>55</sup> Jeffrey M. Jones, "Fewer Americans Now View Their Income Taxes as Fair," *Gallup.com* (April 15, 2013), <http://www.gallup.com/poll/161780/fewer-americans-view-income-taxes-fair.aspx>

<sup>56</sup> And the audit rate for the nation's largest corporations plunged to its lowest level in the last twenty years – approximately 26% – less than half what it was in 1988. Transactional Records Access Clearinghouse, Audits of Largest Corporations Slide to All Time Low, <http://trac.syr.edu/tracirs/newfindings/current/>.

<sup>57</sup> *Id.*

<sup>58</sup> Transactional Records Access Clearinghouse, District Enforcement, <http://trac.syr.edu/tracirs/findings/07/index.html> (last visited Mar. 7, 2009).

theory of economic and political justice as well as a deep familiarity with one or more tax codes, their legislative history, and their enforcement. Other contributions to this volume have touched on such issues.<sup>59</sup> For the moment, I think it is safe to assume that a tax code would have to achieve a fairly high level of unfairness before it could be said that an evader was not cheating.

And what about cases in which a tax evader does not intend to obtain an unfair advantage over others? Here, I have in mind the problem of tax resisters and tax protesters. Tax resisters object to paying taxes that will be used for government activities they oppose, such as waging supposedly unjust wars.<sup>60</sup> Tax protesters claim to believe that the tax law itself is unconstitutional or otherwise invalid. Both could conceivably argue that the reason they are not paying taxes is not that they wish to free-ride on their fellow citizens, but rather that they have some more “principled” reason for doing so.

This argument would be hard to sustain. The fact is that both tax resisters and tax protesters – whatever their motive -- do free ride on their fellow citizens. Some tax resisters refuse to pay all or a portion of the taxes they owe, and instead make an equivalent donation to charity. But the fact that this money is given away, rather than kept, does not mean that the tax resister lacks an intent to obtain an unfair advantage over others. Almost everyone has *some* quarrel with the way their tax revenues are used, and would prefer to give their money to a hand-picked charity instead. Tax resisters get both the benefit of taxes paid by others and the satisfaction of supporting a worthy charity. That sounds like cheating.

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<sup>59</sup> See, e.g., the contributions from Jennifer Bird-Pollan, Patrick Emerton and Kathryn James, Miranda Perry Fleischer, Theodore Seto, and Daniel Shaviro. See also, e.g., Liam Murphy and Thomas Nagel, *The Myth of Ownership: Taxes and Justice* (Oxford University Press, 2002); Steven M. Sheffrin, *Tax Fairness and Folk Justice* (Cambridge University Press, 2013); Alan M. Maslove (ed.), *Fairness in Taxation* (University of Toronto Press, 1993); Louis Kaplow, *The Theory of Taxation and Public Economics* (Princeton University Press, 2010).

<sup>60</sup> See, e.g., *Cheney v. Conn* [1968] 1AER 779 (where party objected to paying taxes that, in part, would be used to procure nuclear arms).

The case against tax protesters is even stronger. Like tax resisters, tax protesters also continue to reap the benefits of citizenship without paying their fair share. Unlike tax resisters, however, tax protesters do not typically maintain the pretense of giving their money to charity. Tax protesters might well believe that the tax laws are invalid, but they could presumably challenge these laws in ways that did not so directly benefit their own pocketbook.

Finally, what about a person who failed to pay the taxes he owed because he believed that “everyone else” or “most others” were doing the same? Would that still be cheating? So long as at least some people were following the rules and paying all the taxes they owed, there is an argument that *X* would be cheating, since he would still be gaining an unfair advantage over the honest taxpayers. On the other hand, recall that cheating requires that the rules be fair and that they be administered in an even-handed manner. In a society in which most people really were cheating on their taxes, and doing so with impunity, it seems unlikely that the tax laws would be being administered in an even-handed manner. In such a case, an argument could be made that *X* was not seeking an unfair “advantage”; rather, he would merely be seeking to negate the “unfair disadvantage” at which he had been placed. What is interesting here is that many people really do rationalize their failure to pay taxes on the fact that “everyone else is doing it.”<sup>61</sup> In a sense, they are arguing that what they are doing is not cheating, and therefore not wrong.

#### **4. Tax Evasion as Disobedience to the Law**

So far, I have considered whether and to what extent the offense of tax evasion is informed by the moral wrongs of stealing and cheating. What remains to be considered is the

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<sup>61</sup> See generally Joel Slemrod, “Cheating ourselves: The Economics of Tax Evasion” (2007), *Journal of Economic Perspectives* 21: 25; Young-dahl Song and Tinsley E. Yarbrough, “Tax Ethics and Taxpayer Attitudes: A Survey” (1978), *Public Administration Review* 38: 442 (1978).

extent to which tax evasion is defined by two other possible forms of moral wrongfulness -- disobedience to the law (considered in this section) and deceptive covering up (discussed in the next).

The Catechism of the Catholic Church has long spoken of “[o]bedience to authority” as the principal ground upon which the obligation to pay taxes is grounded.<sup>62</sup> If that were true, it should therefore follow that the concept of *disobedience* would be a key to understanding why tax evasion is wrong. There are, however, several problems with this approach. First, there is a genuine debate about whether there really is a moral obligation to obey the law.<sup>63</sup> Second, every violation of a just law involves some form of disobedience. The disobedience approach, taken in isolation, therefore fails to explain how the moral content of tax evasion differs from (and is presumably more serious than), say, various trivial regulatory violations. Third, as we saw above, all cheating involves a rule violation. Since the rule at issue in tax evasion is a legal rule, it might seem that the analysis of tax-evasion-as-disobedience would be subsumed by the earlier analysis of tax-evasion-as-cheating.

Despite these objections, I believe that the concept of disobedience does add something of value to the analysis of the moral content of tax evasion. In contrast to the cheating analysis -- which tends to highlight the wrong done, *horizontally*, to the taxpayer’s fellow citizens – the disobedience analysis tends to highlight the *vertical* nature of the wrong (and harm) done to the government, which needs tax revenue to function.

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<sup>62</sup> *Catechism of the Catholic Church* § 2240 (Libreria Editrice Vatican, Provisional Draft, 1992). This paragraph draws on the discussion in Green, *Lying, Cheating, and Stealing*, at 247. There is also empirical evidence to suggest that people who are “rule followers” are more likely to comply with the tax laws. See Kelvin Law and Lillian Mills, “Managerial Characteristics and Corporate Taxes,” [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2302329](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2302329) (finding that corporate managers with military experience were less likely to pursue “aggressive” tax planning than other managers”).

<sup>63</sup> See, e.g., M.B.E. Smith, “Is There a Prima Facie Obligation to Obey the Law?,” 82 *Yale L.J.* 950 (1973).

Moreover, thinking about tax evasion as a form of disobedience also highlights its dual *malum in se/malum prohibitum* character. Crimes have traditionally been said to be *mala in se* if they involve conduct that is wrongful regardless of whether the conduct has been made illegal (murder and rape are good examples); and *mala prohibita* if they involve conduct that is wrong solely, or primarily, in virtue of their being illegal (the best examples here are certain regulatory offenses, like fishing without a license). As I have argued elsewhere, however, there is no such thing as a pure *malum in se* or *malum prohibitum* offense.<sup>64</sup> Even those crimes that can most plausibly be considered *mala in se* are to some extent defined by law. Conversely, even conduct that is most clearly *malum prohibitum* has some non-legal moral content. The point is that *malum in se* and *malum prohibitum* are better thought of as contrasting qualities along a continuum that, to one degree or another, characterize all criminal offenses, rather than as precise categories into which specific offenses either do or do not fit.

Tax evasion seems to fall somewhere near the middle of the continuum between *malum in se* and *malum prohibitum*.<sup>65</sup> On the one hand, the amount of money citizens owe to the government in taxes is determined entirely within a framework of legally defined rules. The wrong of tax evasion thus cannot be defined “prior to and independent of law,” as one commentator has claimed is characteristic of *mala in se* offenses.<sup>66</sup> In that sense, tax evasion reflects a strong *malum prohibitum* character.

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<sup>64</sup> The concepts of *malum prohibitum* and *malum in se* are dealt with in detail in Stuart P. Green, “Why It’s a Crime to Tear the Tag Off a Mattress: Overcriminalization and the Moral Content of Regulatory Offenses” (1997), *Emory LJ.* 46: 1533, 1570–1580. I have written about the *malum in se/malum prohibitum* distinction more recently in Stuart P. Green, “The Conceptual Utility of *Malum Prohibitum*,” forthcoming in *Dialogue: the Canadian Philosophical Review*.

<sup>65</sup> For a similar argument, see Zoë Prebble and John Prebble, “The Morality of Tax Avoidance” (2010), 43 *Creighton L. Rev.* 43: 693, 736-37.

<sup>66</sup> Douglas Husak, *Overcriminalization: The Limits of the Criminal Law* (Oxford University Press, 2008), at 105.

On the other hand, tax evasion also reflects significant attributes of *malum in se*-ness. No modern society could hope to function without a developed system of shared tax burdens. We do not need to know the particulars of a given tax code to know that evading those obligations, and thereby potentially free-riding on others, is normally wrong. In that sense, tax evasion seems significantly more *malum in se* than regulatory offenses like buying pills without a prescription or practicing medicine (competently) without a license.

## 5. Tax Evasion as Deceptive Covering Up

A final piece in the puzzle of tax evasion's moral content is supplied by the concept of deceptive covering up. As noted previously, in some countries, the crime of tax evasion requires not only that the evader purposefully avoid paying taxes owed, but also that he conceal that activity – say, by hiding income, keeping a second set of books, or claiming personal expenses as business expenses.<sup>67</sup> This distinction – between underpayment *simpliciter* and underpayment plus covering up – marks the line between nonpayment of taxes as a misdemeanor or civil wrong and nonpayment of taxes as a serious felony offense.

Are we justified in punishing someone more for not only evading taxes but also covering it up? Elsewhere, I have discussed the role that covering up plays in defining such free-standing offenses as perjury, false statements, obstruction of justice, criminal contempt, and misprision of felony.<sup>68</sup> Each offense allows for the prosecution of offenders who cover up a separate underlying crime. What makes tax evasion apparently unique is that the underlying wrong and its cover up are combined in a single offense. Imposing more serious penalties on tax evaders who

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<sup>67</sup> See above note 28.

<sup>68</sup> See Green, *Lying, Cheating, and Stealing*, at 133-47, 161-92.

try to conceal their wrongdoing thus seems a bit like imposing higher penalties on murderers who attempt to evade discovery, bank robbers who try to get away with their loot, and insider traders who seek to cover their tracks.

So what justification is there for combining the nonpayment of taxes and its cover up in the same offense definition? The best answer I can offer is that *A*'s covering up his tax evasion will often offer strong evidence that *A* did understand what the law required and intended to violate it. Moreover, when nonpayment of taxes is covered up, it's generally more costly for the government to detect, and in that sense more harmful than mere nonpayment.

### **C. The Moral Content of Tax Avoidance**

To this point, I have argued that tax evasion is wrong primarily because it involves a form of cheating (with disobedience to the law and deceptive covering up playing supporting roles). But what about tax *avoidance* – reducing one's taxes by means that, unlike tax evasion, do not involve a violation of the law? Is that wrong too? And assuming it is, is it wrong for the same reasons that tax evasion is wrong, or for different reasons? Strictly speaking, a work that seeks to explain the moral content of tax evasion need not address these issues. But they have puzzled so many commentators for so long that it is worth asking if there is anything in the foregoing analysis of tax evasion that might be helpful in assessing the moral content of tax avoidance as well.<sup>69</sup>

#### **1. Distinguishing Reasonable from Unreasonable Tax Avoidance**

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<sup>69</sup> For a wide-ranging discussion, see Leo Katz, *Ill-Gotten Gains: Evasion, Blackmail, Fraud, and Kindred Puzzles of the Law* (University of Chicago Press, 1996).

Most citizens, whether law-abiding or not, wish to avoid paying the government the maximum amount the tax law might require. Tax evaders pay less by unlawfully failing to pay the taxes they owe. Tax avoiders try to lessen the amount of that obligation through legal means, using various tax avoidance devices such as deductions, credits, and exemptions. This attempt to lessen one's tax obligation through lawful means is referred to, in general, as "tax avoidance."<sup>70</sup>

But within this general category, a basic distinction emerges. Consider two contrasting cases: In one, *A* gives money to a recognized charity, and then claims a deduction on his tax return, thereby reducing the amount of his taxable income. In the other, *B* sells an asset solely for the purpose of taking a tax loss to be set off against ordinary income, and then repurchases it shortly thereafter. In the first case, *A* seems to have behaved in a manner that is consistent with the purpose of the legislation – namely, to encourage taxpayers to make charitable gifts. In the second case, by contrast, *B* seems to have behaved in a manner that is inconsistent with the purpose of the tax provision that allows taxpayers to set off losses against gains in calculating their tax base.

Many tax systems have sought to distinguish between such cases in their general avoidance rules. One formulation can be found in U.K. law. Under the so-called "reasonableness test," a tax arrangement is said to be "abusive" if, "having regard to all the circumstances, entering into the arrangements or carrying them out cannot reasonably be regarded as a reasonable course of action in relation to the relevant tax provisions, having regard to all the circumstances."<sup>71</sup> These circumstances, in turn, include "(a) whether the substantive results of

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<sup>70</sup> The literature on the difference between tax evasion and tax avoidance is immense. For a sampling, see Valerie Braithwaite (ed.), *Taxing Democracy: Understanding Tax Avoidance and Tax Evasion* (Ashgate, 2003).

<sup>71</sup> Sec. 207(2)-(6) FA 2013. For a useful discussion of the economic substance test in particular, see Robert McMechan, *Economic Substance and Tax Avoidance: An International Perspective* (Carswell, 2013).

the arrangements are consistent with any principles on which those provisions are based (whether express or implied) and the policy objectives of those provisions, (b) whether the means of achieving those results involves one or more contrived or abnormal steps, and (c) whether the arrangements are intended to exploit any shortcomings in those provisions.”<sup>72</sup>

This distinction between reasonable and unreasonable tax avoidance seems to fit the two cases described above. The first transaction is consistent with the relevant provisions, is not contrived, and is not intended to exploit any shortcomings in the provisions. It therefore seems to satisfy the reasonableness test. By contrast, the second transaction cannot be regarded as a reasonable course of action in relation to the relevant tax provisions.<sup>73</sup> The substantive results achieved are inconsistent with the policy objectives of the applicable provisions, they involve contrived and abnormal steps, and they are intended to exploit shortcomings in those provisions.

## **2. Why is “Unreasonable” Tax Avoidance Morally Wrongful?**

The distinction just drawn between reasonable and unreasonable tax avoidance seems useful as a descriptive matter, but it fails to explain why, or even if, the first should be viewed as morally neutral or even desirable, and the second as morally wrong. Unfortunately, the notion of cheating – though key to understanding the wrongfulness of tax *evasion* -- seems to have little immediate relevance here. By definition, tax avoidance, whether reasonable or not, involves no

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<sup>72</sup> Id.

<sup>73</sup> Sec. 207(2)-(6) FA 2013. These circumstances, in turn, include (a) whether the substantive results of the arrangements are consistent with any principles on which those provisions are based (whether express or implied) and the policy objectives of those provisions, (b) whether the means of achieving those results involves one or more contrived or abnormal steps, and (c) whether the arrangements are intended to exploit any shortcomings in those provisions.

rule violation. And since there can be no cheating without a rule violation, it seems to follow that tax avoidance is not cheating.

Nevertheless, the idea that the tax law contains rules, and that rules can have significant normative force does point in the right direction. It has often been claimed that unreasonable tax avoidance violates the “spirit” of the tax laws.<sup>74</sup> I think that is basically true. But more needs to be said about exactly why violating the spirit of such a rule should be understood as morally wrongful.

Let us begin with two cases that I shall call “tennis” and “stock investing,” respectively:

**Tennis:** Suppose that *A* and *B* head out to the club on Sunday morning for what *B* believes will be a friendly game of tennis. Ostensibly, they are playing for the normal, socially acceptable reasons that people play such games -- to get some healthy exercise, enjoy the fun of competition, improve their skills, relish the sunny weather, perhaps even entertain onlookers. Now, imagine that *A*, defying *B*'s expectations and social convention, plays much more aggressively than *B* expected: he hits the ball as hard as possible during warm-ups, attempts to intimidate him into losing his cool, challenges every call made by the referee, makes loud, distracting noises when *B* is about to make his shot, aims shots directly at his head, deliberately stalls to slow the game down, and so forth. Is *A*'s conduct morally wrongful?

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<sup>74</sup> See, e.g., Judith Freedman, “Is Tax Avoidance ‘Fair?’,” C.Wales (ed.), *Fair Tax: Towards a Modern Tax System* (Smith Institute, 2008); Hanna Filipczyk, “Why is Tax Avoidance Immoral? Ethics, Metaethics, and Taxes,” SSRN, [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=2515557](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2515557) (Oct. 27, 2104). The idea that unreasonable tax avoidance involves a violation of the “spirit” of the tax laws is related to, though distinguishable from, an idea developed in John Braithwaite, *Markets in Vice, Markets in Virtue* (Oxford University Press, 2005). Braithwaite argues that we can avoid the abusive loopholing that plagues tax rules by supplementing those rules with more general tax principles, such as a “general anti-avoidance principle which states that schemes are illegal when their dominant purpose is a tax advantage, even if the scheme ‘works’ as a shelter from detailed tax rules.” Id. at 149.

Because none of *A*'s behavior (so far as I can tell – I am not a tennis player myself) violates the official rules of the game, we should conclude that he has not cheated.<sup>75</sup> However, he certainly seems to have violated the “spirit” of the rules. Those rules play a role within, and help define, the larger practice of casual Sunday morning tennis games. Within this framework, winning is valued, of course, but only when it is consistent with the larger goals of practice. *A*'s behavior seems at odds with the reasons that people ordinarily engage in such a cooperative venture: having fun, getting exercise, improving their skills. Indeed, it tends to directly undermine the achievement of such goals.

**Stock investing:** The basic purpose of the stock market is often said to be to provide fluid capital to companies that wish to expand their businesses. Individual traders hope to make money in the market by “buying low” and “selling high.” Like tennis, stock investing is a zero sum game: some players must lose for others to win. Traders, of course, must abide by certain rules of conduct. Most famously, they must refrain from trading on inside information. But imagine a case in which *C*, a professional stock trader, though never actually buying or selling on the basis of inside information, engages in so-called high frequency trading, using supercomputers and ultra-fast fiberoptic cables that allow him to make money from small discrepancies in short-term market gyrations, placing stock orders and canceling them immediately if he doesn't see a gain.<sup>76</sup> Has *C* behaved wrongfully?

Once again, it seems likely that *C* has not violated the law (at least as it currently stands); and, therefore, it would be inaccurate to say that he has cheated. Yet, as in the tennis case, his conduct arguably does violate the “spirit” of the rules regarding stock trading, which at some

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<sup>75</sup> See International Tennis Federation Rules, <http://www.itftennis.com/media/194067/194067.pdf>.

<sup>76</sup> For a popular account, see Michael Lewis, *Flash Boys* (Norton, 2014)

basic level are intended to “level the playing field,” by assuring investors that no one will have an unfair informational advantage. Without such a rule, it is possible that small investors would no longer want to invest in the market, and the market itself would suffer. Firms that engage in the sort of tactics that *C* has engaged in arguably undermine the basic purposes of the market. The more pervasive such conduct becomes, the less the cooperative ends of the practice will be served, and the more likely it is that the market will be viewed as so unfair that small investors will stop investing.

So what does all of this have to do with tax avoidance? Like tennis playing and stock trading, taxpaying is both a competitive and cooperative venture. It is competitive in the sense that almost everyone wants to minimize their own individual tax burden, inevitably at the expense of other taxpayers. It is cooperative in the sense that the tax laws are intended to raise revenue for the state that can ultimately be used to further community goals.

And, as in the case of tennis and stock trading, we need to consider the substantive ends that our tax system is intended to serve. A taxpayer who claims deductions and exemptions based on transactions that are consistent with the purpose of the provisions allowing such deductions and exemptions acts in accordance with tax law’s purpose, and thereby does nothing wrong. Indeed, he has performed as the system wants him to do. He has given to charity, bought a house, or put money away for his retirement, and then claimed his deduction. From an ethical perspective, his behavior is analogous to the tennis player who serves the ball hard or the investor who spends long hours poring over a corporation’s fundamentals before deciding to buy or sell shares. None of this conduct is morally wrongful.

By contrast, when a taxpayer claims deductions based on transactions that are inconsistent with the purpose of the law, he disregards the basic rationale of the law, the

substantive ends that the law is intended to serve, the mischief at which it is directed.<sup>77</sup> To understand a rule, as a normative demand, is, or should be, to understand its role within the relevant practice, the reasons that underpin it. To accept a rule as a normative guide must then be to accept it as serving that end, or playing that role -- to accept it and follow it in the spirit in which it was passed. That is how citizens in a tolerably just society *should* relate to the law: not as a set of imposed rules defining a game which they are trying to win -- with tax authorities or fellow citizens viewed as opponents – but, rather, as a way of structuring their shared civic life and of ensuring that the resources needed are raised fairly. Therefore, if one accepts the view that there is a moral obligation to comply with the *letter* of tax laws that are passed in a just manner, it seems to follow that there is also moral obligation to comply with the *spirit* of such laws. Tax avoidance that fails the business purpose test violates that obligation. For that reason, it should be viewed as morally wrong, even though not unlawful.

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<sup>77</sup> I am grateful to Antony Duff for his help in formulating the argument in this paragraph.