

TAX EVASION AND MONEY LAUNDERING

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Abstract: *Tax evasion and money laundering is a process by which one gives or tries to give an appearance of legality to profits obtained illegally by criminals who, without being compromised, subsequently benefit from those revenues.*

The preoccupation of hiding the nature or the existence of money has existed since ancient times. Taking into account the scale of operations and their frequency, specific to those times, the historical tradition enshrines the following practices: the use of banking activities and geographical areas as financial refuge.

The use of banking activities to hide and fraudulently transfer money experienced a special development in the European Middle Ages. These money laundering techniques, which foreshadow modern banking techniques, were mainly designed either to make the high interest rates on loans disappear, hiding their existence, or to appear to be a different kind of income, disguising their nature.

The objectives of tax evasion and money laundering were achieved using several methods:

for long distance payments, between two shopping centers where different currencies were used, the payment amount was calculated on the basis of an artificially increased exchange rate that also covered the payment of interest;

- the amounts paid in excess (the interests) were presented as a special premium to compensate the risks of the loan operation under the justification that the debtor was a bad payer;

- what are now called "ghost companies" were also used. Significant amounts were lent to firms that did not have a real functional role, and then the creditors received a so-called profit from the debtor (which was, in fact, the interest on the loan), even if it did not make any profit and did not carry out no activity.

In essence, all these tricks were intended to deceive the authorities into transfers of the amounts obtained fraudulently, generally through tax evasion.

Key words: fraud, tax evasion, money laundering, banking money laundering

JEL Classification Codes: H20, H30, G28.

1. TAX EVASION - PRECURSOR PHENOMENON OF MONEY LAUNDERING

All the authors who dealt with tax evasion revolve around a range of words that make it very difficult to understand the phenomenon. This shows the complexity of this phenomenon, the difficulty of describing it exactly and completely through a number of words and expressions, and not the inability of specialists to understand and reproduce what the phenomenon consists of. Even the word "evasion", related to "evasive" which means unclear, vague, imprecise, makes us think of the fog in which are often wrapped many actions, acts and deeds that have as their purpose and result evading the legal payment of taxes and fees.



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The taxpayer's relationship with the tax is first and foremost a matter of perception in relation to the entire levy he has to pay. This perception is obviously characterized by a feeling of coercion, even pressure, which explains the permanent opposition (rejection) to the tax.

The taxpayers find certain means, exploit the insufficiencies of the legislation and elude them legally, evading all or part of the payment of taxes, just because of an insufficient legislation. In this way, the taxpayers remain within the limits of their rights, without the possibility of being charged with anything, and the state can only defend itself through clear and precise legislation.

The most frequent cases of evasion arising from the favorable interpretation of tax legislation, in the practice of market economy countries, are the following:

a) establishing depreciation or reserve funds higher than those justified economically, thus reducing the taxable incomes;

b) the practice of some companies to invest part of the profit from the acquisitions of machines and technical equipment for which the state grants reductions of the income tax, a measure meant to stimulate the accumulation;

c) the family associations, as well as the occult societies between the entrepreneur's wife and his children; the result of such a maneuver is their separate taxation, the separate distribution of revenues on each associate leading to the reduction of fiscal burdens;

d) the total income of the family members can be divided equally between them, regardless of the contribution of each one to its realization, resulting the reduction of the income tax, which is due to the state;

e) establishing savings deposits administered by the parent (guardian) in favor of the minor child. In this case, although the income related to the deposit is subject to taxation, the tax paid is lower compared to what would be due on the income thus redistributed;

f) the use, within certain limits, of the legal provisions regarding the philanthropic donations (whether they occurred or not) leads to the deduction of part of the income from taxation;

g) a taxpayer may choose the personal income tax or the taxation system applicable to the income realized by the corporation. Choosing the second tax regime, the taxpayer makes a significant deduction from taxable income because the corporate tax system includes numerous facilities that lead to a substantial reduction of the tax burdens;

h) taking into account some legal facilities regarding the exclusion from the taxable mass of the living expenses, the professional training and the production practice, and the amounts paid for the research contracts having as object the priority programs of national interest;

i) deducting from taxable income of the protocol, advertising or publicity expenses, whether or not they have been made.

“An example of tax evasion under the shelter of the law is the taxation of income earned by certain categories of individuals based on some average income norms, a taxation that allows the taxpayers who earn more than the average income not to pay the tax for that difference” (Gliga, Constantin Ioan, 2017).

The tools of the international tax fraud are limited to three types of companies installed in the countries of refuge: the holding companies, the basic companies and the fictitious companies (sham companies).

The basic companies are companies that do not have their own economic activity. They are created in the countries with a reduced fiscal pressure, to manage the commercial and financial benefits made in other countries by the subsidiaries of the founding group. This type of company is found especially abroad, where the income from foreign sources received by the resident companies is not taxed if they are controlled by non-residents.

The fictitious (screen) companies have a much more insignificant material existence. They have a dual purpose: either to establish in the countries of refuge the profits made from certain operations, or to make more difficult the fiscal control of the accounting of the various enterprises in the group. These companies may be:

- the patent companies in whose name the patents obtained are granted or assigned;
- the auxiliary service companies that invoice at an increased price the services actually provided or the fictitious services. This is especially the case of the market research or advertising companies.

The primary money laundering offenses, included in the Romanian law are: drug trafficking, non-compliance with the regime of weapons and ammunition, non-compliance with the regime of nuclear materials or other radioactive materials, non-compliance with the regime of explosives, counterfeiting coins or other valuables, pimping, smuggling, blackmail, illegal deprivation of liberty, banking fraud, fraudulent bankruptcy, theft and concealment of vehicles, non-compliance with the protection regime of goods, trafficking in protected animals in their countries, trade in human tissues and organs, crimes committed through computers and credit cards, crimes committed by persons who are part of criminal associations, non-compliance with the provisions on the import of waste and residues, non-compliance with the provisions on gambling.

The crime of tax evasion, the corruption crimes, the customs crimes, etc. which "produce" most of the black money, are not considered by the legislator as primary money laundering crimes.

A special problem is that of the phantom companies, the existence of a high level of the underground economy is primarily the result of the operation of such companies.

From the experience so far, the "great specialists" in phantom companies are the foreign citizens. In fact, the huge amounts obtained from the underground economy are exchanged in foreign currency and transferred abroad, without any consideration for these transfers, thus leading to an even greater imbalance of the balance of payments.

2. MONEY LAUNDERING TYPOLOGIES SPECIFIC TO ROMANIA

“Criminals of various categories, whether drug or arms traffickers, smugglers of goods or one of the various types of artists in fraud, must launder the money coming from their crimes, for two reasons. The first is that the very trace of money can become evidence against the perpetrator of the crime; the second is that the money itself can be the target of investigation and confiscation” (Hoanță N., 2010).

The schemes of money laundering have a number of features determined by:

The *jurisdiction* of money laundering – the offenders act according to certain favorable or restrictive conditions of the law and the custom of the place.

The *crime generating illicit funds*. Sometimes, the generating crime creates a special "style" of laundering, transferring its own characteristics to the bleaching process. An eloquent example is that of money laundering from tax evasion.

The *transnational character*. A number of features results from the fact that money laundering takes place within the national borders or the money crosses several jurisdictions. Criminals adapt their mode of operation in order to slip successfully through the various barriers that accompany the external transfers of money.

“It was found that during the activity in the field of preventing and combating money laundering, there are "star" criminal schemes in certain periods, meaning that they are frequently used in a period of time, after which the criminals abandon them and invent others” (David,

Mihail,2008). In Romania, such a "star" scheme was the money laundering from the substitution of petroleum products.

The most common *systems used in money laundering* are:

a) The offshore destinations, respectively those countries or territories that accept fictitious establishments of companies, areas with elastic regulations on foreign exchange control and great tax freedoms offering to the private companies at the same time, almost without exception, an impenetrable banking secret and many rights in this regard. When money is transformed into a form that can be transferred or smuggled, most often it takes the path of an offshore center. Tax havens are one of the most widely used procedures for tax fraud and evasion internationally.

b) The shell companies are those companies that do not have independent assets or commercial operations of their own and that are used by their owners to conduct their business or to maintain control over other companies. A company of this type is registered in the country in which it is established, but is not traded on the capital market and does not operate independently. As these companies are not illegal, the money launderers, the escapists and the terrorist financiers can relatively easily convert and use them to hide their illicit incomes. These companies are easy to set up and can be connected with other fictitious companies in the world. If a company is established in a jurisdiction with a strict legislation of protecting banking secrecy, it is almost impossible to identify the true owners or administrators of the company and therefore it is impossible to pursue the illicit funds that are returned to the real beneficiary.

c) The freelancers, respectively lawyers, notaries, accountants, etc. perform a significant number of activities in support of their clients, organizing and managing their financial and commercial affairs. First of all, they provide assistance to individuals and legal entities in areas such as investments, business start-ups, administration, management, etc. Some of them end up specializing in identifying companies or offshore locations for their use in money laundering schemes, preparing all the necessary specialized documentation, which gives an appearance of legality to the business.

d) The alternative systems of money transmission allow money to circulate around the world, without using the conventional banking system. They can be used for legal and illegal purposes, in various forms. For obvious reasons, these systems are attractive, being widely used by the organized crime networks and dangerous criminals, both to launder proceeds of crime and to avoid taxes and customs duties.

e) The casinos are vulnerable to being manipulated by money launderers due to the speed and intensive nature of cash games, but also because they provide their customers with a wide range of financial services in a large number of countries. Often these services available at casinos are similar to those provided by banks and may include debit or credit accounts, facilities for sending or receiving funds directly from other institutions, foreign exchange and check cashing services.

f) The Internet. The risk of money laundering is very high due to the fact that the Internet offers easy and almost universal access, eliminates face-to-face contact and is extremely fast and efficient in removing borders.

g) The non-profit organizations raise hundreds of billions of dollars annually from donors and distribute this money to their beneficiaries. Both their administrative expenses and the amount and necessity of the beneficiaries' expenses can be exaggerated and their usefulness difficult to appreciate.

The money laundering mechanism involves, basically, *three stages*:

- the separation of money from the source of their illicit origin, which often involves their transfer abroad – the placement;
- hiding their illicit origin and creating an appearance of legal origin, an operation also called "erasure" or "disguise" – the stratification (or the investment);

- the return of the clean money to the offender to use it in terms of legal origin – the integration.

It should be noted from the outset that, depending on various factors (the size of the amount, the permanent or accidental nature of the basic crime, the national law and the time available to the offender), the money laundering may follow a longer or shorter cycle. It can be committed even in the country where the basic crime was committed or involves the transfer of money abroad, its laundering and then the return of funds to the offender's country of residence.

Money laundering, especially internationally, is not usually done directly by the people who are engaged in basic illegal activities, but by some specialized professionals who know the operations on the international capital market, the banking products and services characteristic of some banks in certain countries and which can be used for this purpose. Money laundering professionals have a body of information that allows them to determine the risks of being detected and to exploit the differences between the control regimes, the regulations and rules on the financial-banking supervision in different countries.

Usually these professionals who have a high level of training and professional ability, perform sensitivity analyzes on behalf of those who want to launder money. Through these analyzes, performed in several “route” variants, they usually try to determine two things: the probability that the origin of the laundered money will be detected on a route; they build several routes to be used simultaneously - for the same amount divided in smaller amounts - in order to struggle the risk of identifying the disguised money: several types of investments, several types of banking operations, in several countries, etc.

As long as there are differences between the control and supervision regimes between countries, the objective of money laundering professionals remains to identify them through permanent information and, of course, to capitalize on them.

The mechanism of money laundering can be likened to a cycle through which the money is separated from the offender who obtained it illegally and, after going through some stages, it returns to the offender "clean". Going through these steps involves a cost which, if it amounts to 30% of the total amount and is returned in proportion of 70%, is considered an "efficient" washing operation. There are often cases when this cost is 50% or more.

The fundamental problem in the money laundering mechanism is that in most cases the money in the first stage is acquired in cash. The sale of drugs, for example, is carried out by "street soldiers" who usually distribute them in small quantities, collecting small sums; weapons are traded directly with cash payment, although the amounts collected are high; similarly thye blackmail, the bribery, the prostitution and the pimping are also done primarily through cash payments.

3. CONCLUSIONS

Although progress has been made in this area both in terms of legislation and cooperation between countries, money laundering remains a controversial topic in some areas, and in some countries the jurisdiction still does not consider it a crime in itself, mainly from two reasons:

- the first is determined by the fact that the crime of money laundering is a totally different act and consists of a set of actions that seem innocent and common by their nature, occurring in financial-banking environments, compared to armed robbery or drug trafficking whose harmful, brutal effects are immediately seen and unfold, at least partially, in an area of the underworld. For people outside the law enforcement system, it is not always obvious and clear how much harm has been done by money laundering, who has been harmed (regardless the tax evasion) and therefore why it should be considered a crime;

- the second is determined by the financial interest of those involved as intermediaries in the money laundering process. For certain countries, banks or trusts specialized in such techniques, etc., the huge amounts associated with the money laundering process they facilitate are important sources of income, without any effort, only on the basis of the permissive commercial and banking laws.

In essence, the money, the profit of the operation forms both the motive of the basic crime – the personal enrichment - and the way of constituting the "working capital" for another crime. In the past, those who committed crimes were punished, but those such as directors of companies or banks who tacitly wanted and / or accepted operations remained unpunished. This thinking and practice has been abandoned, for no one has any doubt about the criminal essence of the direct or indirect act of money laundering.

Becoming a dangerous social phenomenon, the money laundering could not but be reflected in the criminal law. Therefore, the criminal law comes to provide support by including the crime of money laundering among those subject to punishment.

According to the Law for preventing and sanctioning money laundering, as well as for the establishment of measures to prevent and combat the financing of terrorist acts, money laundering means:

a) the exchange or transfer of goods, knowing that they come from the commission of crimes, in order to hide or conceal the illicit origin of these goods or in order to help the person who committed the crime from which the goods come to evade prosecution, trial or execution of the sentence;

b) hiding or concealment of the true nature of the origin, location, disposition, circulation or ownership of the goods or of the rights over them, knowing that the goods come from the commission of crimes;

c) the acquisition, possession or use of goods, knowing that they come from the commission of crimes.

Today, "money laundering is not as simple as in the days of the American gangsters, it is a complicated economic and financial process that goes through several stages and involves several people and institutions"(Todosia M.,1992).

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