Global Guide to Criminalization of Tax Offenses - United States

| Contents |
| --- |
| To generate table of contents, right-click here and select **Update Field.** |

This is the **United States** section. Select a topic from the menu and explore the questions within.

# Key contacts

# International Guide on Criminalization of Tax Offenses

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## 1. Please define provide details of criminal tax fraud offence in your jurisdiction

There are a number of tax crimes and related offenses that can be prosecuted. The below represent the felony charges most often brought against high net worth individuals, advisors, and entities.

**Tax evasion (26 U.S.C. §7201)** is the willful attempt to evade or defeat tax. There must be (1) a specifically identified deficiency in tax, (2) an affirmative act that constitutes evasion or attempted evasion, and (3) the actions must be willful (meaning that one must know that there is a legal duty and consciously decide not to obey that duty).

**Subscribing to False Returns/Documents; Aiding and Abetting the Preparation of a False Return or Document (26 U.S.C. §7206)** are false statement-type offenses. Subscribing a false return requires: (1) a belief that the return or document is not true and correct; (2) willfulness (as per above); (3) materiality of the false statement (though knowledge that the statement is material is not necessary); and (4) signing/submitting the document under penalty of perjury with the IRS.  For aiding and abetting: (1) the person must aid or assist in preparing the return of document; (2) the return must be fraudulent or false as to a material matter; and (3) the person must have had an intent to defraud the government (willfulness).

**Conspiracy to Defraud the United States (18 U.S.C. §371)** is a general fraud statute (not specific to tax) under the federal criminal code. The offense consists of (1) an agreement between two or more parties, (2) to commit an offense or defraud the United States, (3) an overt act by at least one of the parties in furtherance of the conspiracy, and (4) an intent to defraud or commit the underlying offense. This provision is typically used to prosecute advisors (such as accountants, lawyers, or bankers) who create schemes to help taxpayers evade tax or who otherwise take affirmative steps to help taxpayers hide their taxable income.

**Mail and Wire Fraud (18 U.S.C. §§1341 and 1343)** are also general fraud statutes. The elements are (1) voluntary and intentional participation in a scheme to defraud others; (2) an intent to defraud; (3) reasonable foreseeability that interstate mail or wire communications (wire, radio, or television) would be used in furtherance of the scheme; and (4) actual use of mail or wire communications as part of the scheme. Historically, the U.S. authorities did not charge mail and wire fraud based on tax crimes but recently the Tax Division has begun to take a different view in these charging decisions.

**Willful Failure to Collect or Pay Over Tax (26 U.S.C. §7202)** is charged against those who are responsible for collect and transmitting tax on behalf of other taxpayers (such as withholding and payroll taxes). There are two separate offenses – one relating to failure to collect and another relating to failure to account for and pay over tax. There must be: (1) a duty on the defendant's part to collect tax or account for and pay over tax, (2) a failure to so collect tax or account for and pay over the tax, and (3) knowledge of both the duty and the violation of the duty (willfulness). This is typically only charged in cases of fraudulent employment companies who contract to provide employees to third party employers and then fail to withhold (or withhold and fail to pay over) employment taxes.

Other general criminal offenses that are employed in tax-related cases include: (1) Making False Statements (18 U.S.C. §1001) (knowingly or willingly making of a false or fraudulent statement about a material matter within the jurisdiction of the agency to which the statement was made); (2) Making False, Fictitious or Fraudulent Claims (18 U.S.C. §287) (presenting a claim against the United States that the person knows is false, fraudulent, or fictitious at the time the claim is submitted); and (3) Aiding and Abetting (18 U.S.C. §2) (derivative liability for a person who aids, abets, procures, or otherwise induces the commission of any federal crime, or otherwise causes another to commit a federal crime).

## 2. What are the typical trigger points that could lead to criminal investigations? Can the application of certain tax penalties trigger criminal proceedings?

There is no specific adjustment that will trigger criminal investigation. Criminal charges can be brought regardless of the amount of any underpayment of tax. Certain criminal violations do not require a finding that any adjustment in tax due is necessary. However, referral for criminal investigation and or prosecution will become more likely the larger any underpayment is and the more egregious the conduct is in failing to comply with the law.

## 3. Can a certain amount of tax adjustment trigger criminal proceedings for tax fraud?

No tax penalties automatically trigger a criminal investigation or criminal charge. However, the civil fraud penalty is typically applied in a case that is investigated or charged criminally. Internal procedures at the IRS and the Justice Department generally hold that a criminal case will not be brought or pursued if there is not sufficient evidence to sustain a civil fraud penalty.

## 4. Is criminal intention a requirement, or can mere negligence be the basis of a criminal offence?

Intent or willfulness is required to sustain a criminal charge. Negligence alone, even gross negligence, is not sufficient to bring a criminal prosecution under US laws. Willfulness generally requires an intentional act (or omission) in violation of a legal duty. However the accused does not necessarily need to have knowledge that the act is criminal. Reckless disregard of the truth or failure to inquire into underlying facts can serve as a defense to liability, though purposefully contriving to avoid learning the facts can, on rare occasions, undermine that defense.

## 5. Does the spontaneous filing of an amended tax return (either through a self-disclosure mechanism or not) have an impact on the initiation of criminal proceedings? Is full payment of tax required?

The general practice of the IRS is to not refer a case in which a taxpayer files an amended return and makes full payment or makes payment arrangements before the IRS has initiated an audit or otherwise received information alerting them of the improperly reported items.

## 6. Can the prosecutor, on their own initiative, prosecute the tax fraud offence?

Tax fraud and other tax crimes are prosecuted only after, or as a part of, signing off on the matter by both the Criminal Investigations Division of the IRS and the Tax Section of the Justice Department. It depends on which U.S. Attorney’s Office is involved whether cases are run “administratively” (directly by the IRS) or through the grand jury process (although all USAOs can and will do both). Ultimately, the Tax Section evaluates the case and determines whether it should be referred for prosecution to the US Attorney's office in the location that has jurisdiction. Then the USAO has to agree to take the case (which is often, but not always, a foregone conclusion).

## 7. What is the statute of limitation period applicable to the tax offences in your country?

The most frequently charged criminal tax offenses are subject to a specific statute of limitations of six years. The general statute of limitations for federal criminal offenses is five years from the date of the offense. The limitations period for each criminal offense is:

Tax Evasion – six years

Subscribing False Returns; Aiding and Abetting False Return – six years

Submitting Fraudulent Returns – six years

Conspiracy to Defraud – six years

Mail and Wire Fraud – five years (10 years if the fraud affects a financial institution)

Willful Failure to Collect or Pay Over Tax – six years

Willful Failure to File a Return or Pay Tax – six years

Making False Statements; Making False, Fictitious or Fraudulent Claims – five years

Aiding and Abetting – same as the underlying offense that was aided.

## 8. When does the statute of limitation period start to run e.g., filing of a tax declaration, failure to pay tax by deadline, tax assessment as a result of a tax audit, etc.?

The running of the statute generally begins once the crime is "completed." Generally, the crime is completed at the following points for the criminal offenses discussed:

Tax Evasion – the later of the date the return is filed or the date of the last affirmative act in furtherance of the evasion.

Subscribing False Returns; Aiding and Abetting False Return – the date of filing of the return or document (not the due date of the return).

Submitting Fraudulent Returns – the date on which the affirmative act of discovery or disclosure occurs.

Conspiracy to Defraud – the date of the last act in furtherance of achieving the central aim of the conspiracy. In the case of tax evasion, that can include false statements or other actions after the filing of a return in order to conceal the fraudulent or improper items reported.

Mail and Wire Fraud – the date of the last use of the mails or wires in furtherance of the scheme to defraud.

Willful Failure to Collect or Pay Over Tax –the date the tax is due.

Willful Failure to File a Return or Pay Tax – the date the return is due (including extensions) or the date the tax is due (including extensions).

Making False Statements; Making False, Fictitious or Fraudulent Claims; Aiding and Abetting – the date on which the statement or claim was made or the date on which the aid was provided.

## 9. What criminal sentences [e.g., custodial, criminal fines or others ] may be incurred in case of a conviction for tax offenses in your jurisdiction?

Most tax crimes can be punished by fines and/or imprisonment. The general maximum fine for tax offenses is USD 250,000 for individuals or USD 500,000 for corporations.  Imprisonment is governed by the Federal Sentencing Guidelines which set a baseline term of imprisonment to be adjusted by the sentencing judge (who typically sentences below that “guideline range”). As a very general matter, setting aside various specific adjustments, the guidelines are driven by the amount of tax loss with tax losses in excess of USD 550,000 often resulting in a calculation -- for a first time offender -- of a custodial sentence.

Tax crimes also have a “statutory maximum” enacted by Congress. This maximum cannot be exceeded regardless of the tax loss. Due to flexibility in charging decisions, this maximum is rarely a functional limitation on a creative prosecutor faced with a large tax loss.

Tax Evasion – Fine and/or up to five years imprisonment.

Subscribing False Returns; Aiding and Abetting False Return – Fine and/or up to three years imprisonment.

Submitting Fraudulent Returns – Fine (up to USD 100,000 for individuals or USD 200,000 for corporations) and/or up to one year imprisonment.

Conspiracy to Defraud – Fine and/or up to five years imprisonment plus restitution for any losses caused by the scheme to defraud.

Mail and Wire Fraud – Fine (up to USD 250,000 or USD 1,000,000 if a financial institution is affected) and/or up to 20 years imprisonment (30 years if a financial institution is affected).

Willful Failure to Collect or Pay Over Tax – Fine and/or up to five years imprisonment.

Willful Failure to File a Return or Pay Tax – Fine and/or up to one year imprisonment.

Making False Statements – Fine and/or up to five years imprisonment.

Making False, Fictitious or Fraudulent Claims – Fine (up to USD 1,000,000) and/or up to five years imprisonment.

Aiding and Abetting – same as the underlying offense that was aided.

## 10. Can having a compliance or risk mitigation program in place mitigate criminal liability for a Company in your jurisdiction?

Having a compliance program reduces the likelihood of willful conduct occurring in the first instance. To that extent, it is helpful. It is, however, no defense to charges.

## 11. Is there a formal or informal program allowing individuals or entities to self-disclose criminal conduct and block prosecution? If not, does such a disclosure mitigate the likelihood of prosecution or reduce the potential sentence and fines?

The IRS and Treasury have developed several formal self-disclosure programs relating to various initiatives, such as the effort to bring taxpayers with foreign financial accounts and income into compliance. There is not a formal self-disclosure program that completely bars criminal charges by rule. However, the IRS will generally not refer a case for criminal prosecution where a taxpayer files an amended return correcting all improper items and makes full payment (or makes arrangement for payment) before the IRS initiates an audit or otherwise receives information alerting them of the improperly reported items.

## 12. Once the criminal proceeding has been initiated is there an impact in terms of liability in case of full payment of a tax assessment issued by the tax authorities (first-time offender rule)?

No – criminal liability is not affected by full payment after the proceedings are initiated. However, such payment may be a factor in determining either sentence upon conviction, or the prosecutor's willingness to enter into a plea agreement or other negotiated conclusion to the proceedings.

## 13. Does criminal prosecution of a tax offence have an impact on the tax authorities' statute of limitation period?

It depends. Criminal prosecution itself does not alter the civil statute of limitations. In cases of fraud the government is not subject to a limitation period for the assessment and collection of additional taxes relating to the fraudulent items. In the case of a criminal conviction for a fraud offense, that conviction will serve as proof that the unlimited statute of limitations for fraud applies to any items that were the subject of the conviction. Absent a conviction, the government can allege fraud and the applicability of the unlimited statute of limitation in a civil case for assessment and collection, but must prove fraud (although to a civil, lesser, standard) in that case.

## 14 Can the tax authorities assess and collect underpaid taxes even if the case becomes criminal

Yes. Civil enforcement of alleged tax deficiencies are not restricted by criminal proceedings as a matter of law. However, because a conviction for fraud will constitute conclusive proof of fraud, extending indefinitely the statute of limitations on assessment and collection, and plea agreements or sentences can encompass restitution and/or tax loss findings that make assessment and collection easier, civil enforcement historically was stayed during the pendency of criminal proceedings. This is, however, not the case with respect to certain marketed tax shelters where the prosecutors are targeting the promotors while the IRS goes after the taxpayers for civil tax liability and fines.

## 15. Is it possible to reach a tax/criminal settlement with the tax authorities/public prosecutor/judge?

Taxpayers can negotiate and enter into plea agreements with the prosecutors to resolve criminal tax charges. The Justice Department has outlined guidelines relating to plea agreements. Those guidelines generally provide that prosecutors “should charge and pursue the most serious, readily provable offenses. By definition, the most serious offenses are those that carry the most substantial guidelines sentence, including mandatory minimum sentences.”  Prosecutors "will generally seek a plea to the most serious offense that is consistent with the nature and full extent of the defendant's conduct and likely to result in a sustainable conviction, informed by an individualized assessment of all of the facts and circumstances of each particular case.”

In general the following elements will be present in a plea agreement to a criminal tax charge:

Guilty plea to the Major Count (as designated by the prosecutors when charging, typically this is tax evasion).

Tax loss, including loss from all potential counts, plus losses from relevant conduct.

Waiver of appeal.

An admission of either the receipt of enumerated amounts of unreported income or enumerated amounts of claimed illegal deductions or improper credits for specified years in issue.

A stipulation that the defendant is liable for the civil fraud penalty imposed by §6663 on the understatements of tax for the years involved.

An agreement by the defendant to file, before sentencing, complete and correct initial or amended tax returns for the years in issue and, if requested, to provide the IRS with information regarding these years and pay at sentencing all additional taxes, penalties, and interest due and owing.

Agreement by the defendant not to file thereafter any claims for a refund of taxes, penalties, or interest for amounts attributable to the returns filed incident to the plea.

Agreement by the defendant to sign a waiver with the IRS contemporaneously with signing the plea agreement, allowing the IRS to assess and collect enumerated amounts of tax due and owing for specified years in issue.

## 16. Who can be prosecuted: just individuals/directors or also companies?

Both - Corporates and Individuals

Companies can be prosecuted for tax crimes, but due to issues of proof and the nature of corporate persons, such prosecutions can be difficult. Generally all elements of a crime must be present via the acts or omissions of corporate agents who were acting within the scope of their employment. Commission of those acts must be authorized, performed, or at least tolerated by the Board or senior managers. In addition, the employees cannot be acting against the interest of the corporation – in other words, there must be some arguable benefit to the corporation from the acts.

The Justice Department has formulated binding guidelines applicable to decisions to indict corporate entities for tax crimes. The guidelines look to certain factors when determining whether a charge against the corporation should be made:

the nature and seriousness of the offense, including the risk of harm to the public, and applicable policies and priorities, if any, governing the prosecution of corporations for particular categories of crime;

the pervasiveness of wrongdoing within the corporation, including the complicity in, or the condoning of, the wrongdoing by corporate management;

the corporation's history of similar misconduct, including prior criminal, civil, and regulatory enforcement actions against it;

the corporation's timely and voluntary disclosure of wrongdoing and its willingness to cooperate in the investigation of its agents;

the existence and effectiveness of the corporation's pre-existing compliance program;

the corporation's remedial actions, including any efforts to implement an effective corporate compliance program or to improve an existing one, to replace responsible management, to discipline or terminate wrongdoers, to pay restitution, and to cooperate with the relevant government agencies;

collateral consequences, including whether there is disproportionate harm to shareholders, pension holders, employees, and others not proven personally culpable, as well as impact on the public arising from the prosecution;

the adequacy of the prosecution of individuals responsible for the corporation's malfeasance; and

the adequacy of remedies such as civil or regulatory enforcement actions

## 17. Can foreign employees/directors be prosecuted?

Yes, fraud or evasion of US taxes can subject a foreign employee or director, as well as foreign corporation, to criminal liability. This is, however, unlikely absent particularly egregious (and certainly willful) conduct on behalf of that foreign employee or director.

## 18. In case of an employee / director being prosecuted in connection with the lack of payment of Company's taxes, is the Company liable for the amounts claimed to such individual?

The company would remain liable for any of its taxes that were not paid, however, the company is not liable for penalties or fines that might be levied against the employee or director because of the employee/director's own individual acts.

## 19. Have you seen an increase of criminal prosecution for tax offenses over the last five years in your jurisdiction? If so, in relation to what topics?

No. In fact, enforcement activity, both criminal and civil, has decreased over the last several years. However, increased funding for enforcement included in the Inflation Reduction Act signals that this trend may reverse in coming years.

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