

THE DIMENSION OF TAX EVASION IN ROMANIA

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Tax evasion is currently a complex economic and social phenomenon encountered both nationally and internationally. Tax evasion is one of the most important divisions, among the most studied, analyzed, researched in the public finances and within the fiscal and financial law, both by the specialists dealing with theoretical problems, as well as by those dealing with the activity of research, design and technical execution. However, despite everything written about the causes, procedures, size, control, or sanctions related to tax evasion, the words that indicate this phenomenon are inaccurate and the field is relatively uncertain.

Key words: *tax evasion; public finances; shadow economy*

JEL Classification: *H 26*

I. INTRODUCTION

It is well known that tax evasion is massive in the economies/societies with weak institutions, where respect for the law is distorted, as well, by a bad relationship between the state and the citizen. The payment much under the legal provisions of tax obligations (taxes and fees) is linked to the operation of a broad underground sector that includes activities under the law (16). One of the strongest measures that the European Commission has taken to combat the crisis of confidence across the continent was **1164 Directive of July 2016**. Broadly, it sets the general framework that allows governments to combat tax evasion by multinational companies. The original source of this directive was, however, an OECD study, which highlighted that, due to legal evasion of multinationals, domestic budgets are losing annually an estimated amount of \$100 billion to \$240 billion globally. A pretty vague estimation of course. However, there was a widespread agreement among the **OECD** countries and within the **G20** regarding the fact that the rules should be changed globally. Journalistic investigations concerning tax havens were, moreover, initiated precisely in the wake of these new guidelines (**Annual Report, Romanian Fiscal Council, 2016**).

In 2016 Romania's economy recorded the highest rate of economic growth in the post-crisis period of 4.8%, the real gross domestic product (GDP) in 2016 being 9.0% higher than in 2008. The main contribution came from the final consumption expenditure of the population (+4.6%), supported by pro-cyclical fiscal policy and rapid salaries increases, while gross fixed capital formation had a contribution of -0.8%, the decrease being determined, exclusively, by the evolution of public investments which contracted by about 24.3% in real terms (**Annual Report, Romanian Fiscal Council, 2016**).

In 2006-2015, Romania pursued a pro-cyclical fiscal policy, stimulating intensively, but unnecessarily and counterproductively, the economy during the expansion periods (2006-2008) and slowing down in the periods operating under its potential (2010-2015) contributing to the amplification of the economic cycle fluctuations and to the accentuation of the imbalances accumulated in the economy (**Annual Report, Romanian Fiscal Council, 2016**).

Tax evasion can be defined as the totality of licit or illicit procedures by which individuals or legal persons are shirking altogether or in part the taxable substance, and consists of the taxpayer's failure to pay the taxes" (**Pantea, 2010**). The definition covers both, legal and illegal means, used by taxpayers to avoid tax laws.

The doctrine comes with another type of definition of tax evasion, presented as follows: "the set of deliberate evasion of tax obligations payment, not committed by direct violation of the law, but by its circumvention by means of simulated and, only, apparently real acts". Analyzing the previous definition, we realized that it does not fully cover the facts because it refers to legal tax evasion. Maurice Duverger addresses tax evasion, as a generic term designating the manifestation of escape from tax. Both, M.C. by Brie and P. Charpentier, considered tax evasion as "the art of avoiding falling into the field of tax law attraction" (**Brie and Charpentier, 1993**).

II. TAX FRAUD AND TAX EVASION

There is, often, a terminological confusion between tax fraud and tax evasion, so a clear distinction must be made between these terms. Thus, tax fraud in a strict sense is a flagrant breach of the law by the taxpayer, from the payment of tax obligations. In other countries, for example in Netherlands, tax fraud, it is meant to present false documents or to disregard the legal obligation to provide the administration with certain information necessary to establish or to control the tax (**Hoanță, 2010**). Under German law, it is considered as fiscal fraud the intention to deliberately omit the evidence, to the administration, of the elements which condition the calculation of the tax or the provision of incorrect or false documents if they would lead to a tax reduction or to obtain unjustified tax advantages (**16**).

An analysis of the US Federal Tax Course captures that the tax literature on tax evasion and fraud is abundant, and yet there is no clear indication of the differences between them. *Tax avoidance* is the minimization of excess taxation by using acceptable, real variants and the *tax evasion* is determined by taxpayers or their professional counselors concerned with the intention to not take into account the tax law in force (**Hoanță, 2010**). In many circumstances, the sketch of evasion is expressed in a non-reality version.

In the conception of the authors N. Hoanță and D. D. Șaguna, tax avoidance can take place in the following ways:

- *tax law ensures itself evasion through a tax regime of favor;*
- *the taxpayer's failure to perform (carry on) the activity subject to taxation;*
- *use of fiscal system gaps (Balaban, 2003).*

It is noted that a key factor in the emergence and development of tax evasion and fraud in any economy is the *fiscal pressure*. Fiscal pressure is, in fact, the integral field of any economy, who deals with tax and fees, their regulation and the way they are applied. Irrespective of this pressure intensity, any government sees itself, permanently, in the position of balancing a situation that has, on a side, the state own interests in the budget, therefore a fiscal pressure as large as possible to cover the interests of the state, and on the other hand, the interests of the citizen who, for obvious reasons, want a lower fiscal pressure. However, we look at this issue, fiscal pressure represents the idea of duty/obligation, through taxes and fees to the state (**Trif, 2015**).

In conclusion, tax evasion is an economic and social process of great intensity with which the countries are confronted and whose undesirable pursuits seek to limit more and more, eradication being unfeasible. The effects of tax evasion are personally resorted to fiscal revenues, leading to abnormalities in the market mechanism and participating in social inequities. The state has the duty to systematically and effectively deal with avoiding and reducing the phenomenon of tax evasion.

This, through the power invested, has the potential to incite tax evasion, having two objectives: a positive one, supported by the desire to encourage capital formation and a negative one, reflected in the support of interest circles, often of the mafia-style.

III. EVOLUTION OF TAX EVASION IN ROMANIA

The phenomenon of tax evasion is difficult to prevent and to quantify for many reasons, including: numerous defects and peculiarities in the field of tax legislation, the organization of fiscal activity, the non-use of the national accounting methodology for macroeconomic evidence, mass evasion by different interest groups, economic agents who know how to take advantages of the law gaps, the principle of banks' confidentiality, etc (**Grosu and Socoliuc, 2008; Bostan et al. 2008**).

According to Eurostat statistics, it is noted that "although the underground economy has a slight downward trend in Romania, its level continues to be at a high point compared to the European average (18.4%)".

"In Romania there is a diversification of the forms of manifestation and propagation of the economic and financial crime, both in terms of tax frauds and undeclared work (black/gray work), through new operating methods, generating direct negative effects on the general consolidated budget of the State, on the stability and the competitiveness of the business environment" (**MAI, 2015**).

Although the phenomenon of tax evasion has decreased slightly as a result of the institutional/legislative measures taken by the authorities, as well as the restraint of the financial markets during fiscal constraints period, it does not cease to damage the general consolidated budget of the state.

This subchapter deals with the phenomenon of tax evasion in Romania, highlighting the most frequent ways of producing tax evasion. As a result, the tax evasion achieved by VAT is the first. This is often done through VAT fraud on intra-community transactions, which is a quite classic method of evasion, through illegal VAT refunds, by lowering the value of goods in custom by the method of insolvency and by the most popular method of fraud, *carousel*.

Throughout the analyzed period, VAT tax evasion has been increasing, from 5.32% of GDP in 2000 to 12.21% of GDP in 2013. Social contributions also produce a large part of tax evasion, ranked second within the period 2000-2013, from 2.33% of GDP in 2000 to 2.43% of GDP in 2013. This is due to the phenomenon of black work/undeclared work that has grown in recent years in Romania.

The following areas generating tax evasion are income tax, respectively profit tax evasion, as well as the excise duty and vice tax evasion. Cigarette smuggling averaged around 20% of the market in 2003-2012. As a share of GDP, this type of tax evasion is increasing, in 2000 the percentage is 0.17% and in 2013 0.23%. With regard to alcohol evasion it is decreasing, the percentage recorded in 2000 being 0.26%, and in 2013 being 0.16%.

At a press conference of the National Council of Small and Medium Enterprises in Romania, it was estimated that the underground economy is made at about 2/3 of undeclared work and the remaining 1/3 of the revenues not reported by enterprises.

Table 1. The size of the black economy, Romania and EU-28 in the period 2003-2015 (% of GDP)

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
RO	33.6	32.5	32.2	31.4	30.2	29.4	29.4	29.8	29.6	29.1	28.4	28.1	28.0
EU-28	22.6	22.3	21.8	21.1	20.3	19.6	20.1	19.9	19.6	19.3	18.8	18.6	18.3

Source: Schneider, F., Raczkowski, K. and Mroz, B, *Shadow Economy and tax evasion in the EU. Journal of Money Laundering Control*, Vol. 18 (1), pp. 34-51, 2015.

We can see from the table below that the size of Romania's black economy, compared to the European Union average, is about 10 percent higher, which is worrying. Although the size of the underground economy has declined throughout the period under review, Romania continues to hold a fairly high share, recording in 2015 a share of 28% of GDP.

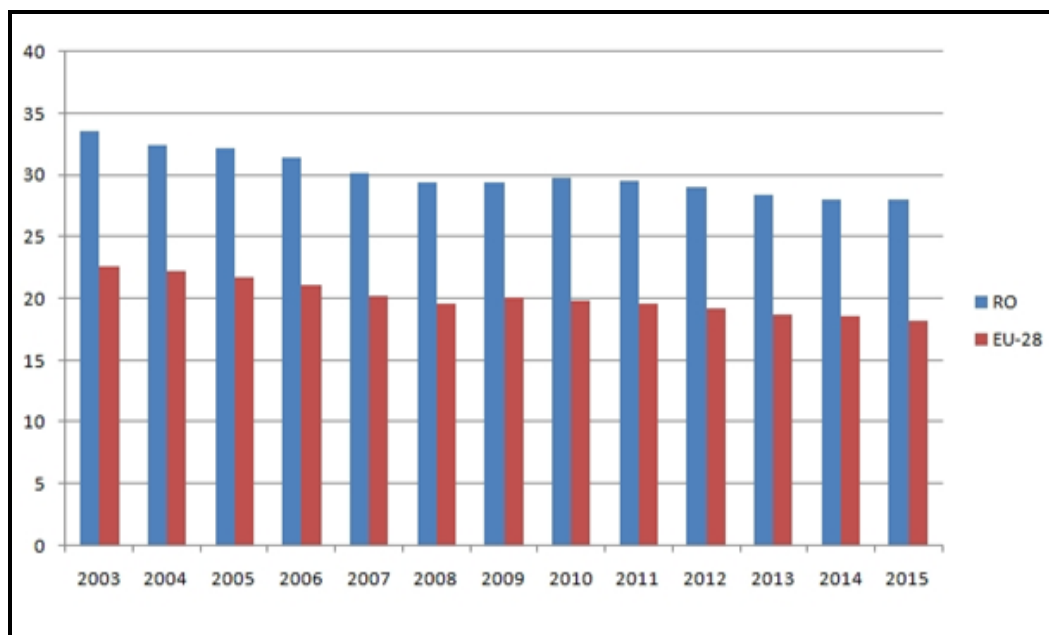


Figure 1 - The size of the black economy, Romania and EU-28 in the period 2003-2015

Source: Schneider, F., Raczkowski, K. și Mroz, B, *Shadow Economy and tax evasion in the EU. Journal of Money Laundering Control*, Vol. 18 (1), pp. 34-51, 2015.

It can be said that Romania's situation regarding the underground economy is worrying, its average over all the years of analysis being higher than the EU-28 average. Romania's underground economy accounted for 28% of GDP in 2015, according to the European Commission.

Romania has cut its underground economy by 4.4 percentage points in the last 10 years, mainly due to preparations for EU membership and the rapid expansion of electronic payment services. Romania's non-observed economy is 10 percentage points above the European average and has the second highest level in the EU after Bulgaria (30.6% of GDP in 2015).

The explanations regarding the causes of tax evasion in the case of Romania are, according to Comaniciu, the following: the misunderstanding of the tax authorities regarding the reasons why the taxpayer avoids the tax system, the existence of tax legislation with gaps, inconsistencies, ambiguities, weaknesses and repeated changes, the ineffectiveness and the inefficient use of public funds, the existence of a precarious financial situation among taxpayers, the ineffectiveness of guidance and assistance granted to taxpayers, the inefficiency of fiscal control, the existence of a low tax education (**Comaniciu, 2017**).

The analysis of the phenomenon of tax evasion also concerns the interactions between creative accounting, management and tax fraud. Tax fraud can also be seen through binomial light: creative accounting (to the extent that it violates tax laws) and organization management.

According to some authors, creative accounting is generated by the management contract (**Dinga, 2008**). According to the rule of meeting the performance criteria (influencing personal income and further professional development), managers of organizations are using a range of accounting procedures and techniques, located on the border between licit and illicit.

IV. CONCLUSIONS

Romania's situation regarding the underground economy is worrying, its average over all the years of the analysis, being higher than the EU-28 average. Romania's underground economy represented 28% of GDP in 2015, according to the European Commission. Romania's non-observed economy is 10 percentage points above the European average and has the second highest level in the EU after Bulgaria (30.6% of GDP in 2015).

Tax evasion is a component of the underground economy that is at the intersection of the underground economy with the formal economy. Regarding combating tax evasion, this can be done through fiscal policy measures and through specialized agencies authorized to prevent and combat tax evasion.

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