

TAX EVASION – FROM ITS ROOTS TO ITS BRANCHES

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Tax evasion is a mass socio-economical phenomenon that is present at a global level, negatively affecting state economies. This article presents and explores the aspects that lead to the manifestation of this phenomenon and the consequences it has on the social and economic environment. The identification and illustration of the determinants and effects of tax evasion are presented by use of an exploratory instrument that is the tree-diagram. The main contributions to the research field this study brings are the labeling, individualization and exploration of the main causes of tax evasion, and also of its consequences, an approach that is essential in order to find solutions for measuring and maintaining a controlled dimension of this phenomenon, which cannot be directly quantified.

Key words: *accounting information; corruption; fiscal pressure; tax evasion; tree diagram.*

JEL Classification: *H26, H30, M49*

I. INTRODUCTION

The relevant tax research studies and literature contain various definitions of tax evasion, some divergent and some convergent, which have the following common points: tax evasion implies the financial deprivation of state budgets, it involves the manifestation of one's volition, that is the showing of intent, qualified by purpose – fully or partially evading the fulfillment of tax obligations, and it cannot be directly quantified or observed.

Moreover, tax evasion is defined as having either a legal or an illicit character, depending on the way in which it manifests itself.

The **European Commission** differentiates three major avenues available to tax evaders:

- Tax fraud and tax evasion, such as not reporting income, thus illegally depriving public budgets of money;
- Tax havens, which imply storing money offshore, where it is unreported and untaxed;
- Tax dodging, often by aggressive tax planning by legal or natural persons, which exploit the limits of the law with the aim of minimizing the taxes to be paid.

In our opinion, tax evasion can be defined as deliberately breaking the law, in order to obtain monetary benefits that lead to the deprivation of the general state budget, by tax noncompliance (avoiding or evading tax obligations) through certain actions or inactions.

In order to properly understand and fight against this phenomenon, what determines its manifestation is of concern. Thus, (**Jackson and Milliron, 1986**) were among the first ones to analyze and debate in their scientific papers the determinants of tax evasion. According to them, there are 14 determinants that can be grouped in three main categories, as follows:

- Demographic determinants – age, gender, education and occupational status;
- Economic determinants – income level, income source, marginal tax rates, sanctions and probability of detection;
- Behavioral determinants – complexity, fairness, revenue authority contact, compliant peers and ethics or tax morale.

Other classifications (**Khlif and Achek, 2015**), made considering the relevant tax literature, divide the key determinants of tax evasion into four large categories:

- Demographical: criminality level, gender, age, education, religion, etc.;
- Cultural and behavioral: tax morale, uncertainty avoidance, individualism, masculinity, power distance, etc.;

- Legal and institutional: law efficiency, bureaucracy, corruption, tax complexity and fairness, democracy, etc.;
- Economical: economic development, economic freedom, etc.

Moreover, other research studies have identified other determinants of tax evasion, as follows: tax morale, public governance, the happiness and wealth of a nation (Achim, Borlea et.al., 2016), tax pressure and the pressure of the complex fiscal rules and regulations (Kirchler, 2007), business culture and social expectations (Cule and Fulton, 2009), and others.

Table no. 1: Overview of some empirical studies identified in the relevant literature regarding tax evasion

Studied variables	Research findings
- the relationship between tax evasion and the economic freedom index, the equity market, the level of crime and the effectiveness of competition laws (Riahi-Belkaoui, 2004)	- a high economic freedom index, equity market and the effectiveness of competition laws are positively associated with tax compliance, while a high level of crime reduces the compliance
- the relationship between tax evasion and bureaucracy and corruption (Picur and Riahi-Belkaoui, 2006)	- low levels of corruption are positively associated with voluntary tax compliance, while a high level of bureaucracy implies a high level of tax evasion
- the relationship between tax evasion and Hofstede’s cultural dimensions (uncertainty avoidance, individualism, masculinity and power distance) (Tsakumis, Curatola et al, 2007)	- uncertainty avoidance and power distance are positively associated with tax evasion, while individualism and masculinity are negatively associated with tax evasion

In our opinion, the tax evasion phenomenon is generated by a vast series of factors having different origins, starting from subjective factors, that reside in the desire to gain large amounts of money or valuable goods in a short period of time, legislative gaps and uncertainty, a tolerant attitude of the society towards breaking of the laws, not knowing or ignoring the fiscal laws, and the tax obligations that result from them, and others, some of which will be analytically presented in the following sections.

II. THE CONNECTION BETWEEN TAX EVASION AND THE ACCOUNTING INFORMATION

Usually “the analysis of the phenomenon of tax evasion also concerns the interactions between creative accounting, management and tax fraud” (Grosu, 2018). In this context, we believe the overview of some aspects that concern the connection between tax evasion and the accounting information is appropriate.

Taking into account the strong relationship between accounting and taxation (Bunget and Dumitrescu, 2008; Paliu-Popa and Ecobici, 2007, Fekete et al, 2009), many times, the accounting information is manipulated, in the sense that it does not reflect a fair and true image of the entity’s financial performance and position anymore, but an image that is desired to be reflected by some users of the financial and accounting information, thus creating the necessary means and mechanisms for evading or avoiding the fulfillment of tax obligations and duties that lead to the acquirement of unjust monetary benefits for the perpetrators of tax evasion.

Thus it can be stated that, when tax evasion manifests itself, the clues and evidence of the existence of this phenomenon are contained within the information that emerges from the accounting information system.

The financial and accounting information is the binder that connects the source documents containing the details to substantiate a transaction entered in the accounting system and which can contain clues or evidence regarding the taxpayers’ actual financial and economic transactions (Dinga, 2008), being the starting point in the investigations to be carried regarding the reality of the transactions recorded into the accounting books, or regarding the omission of registering certain transactions that lead to, entirely or partially evading computations, reporting and payment of taxes due to the general state’s budget.

The clues regarding the commitment of tax evasion crimes can be contained both within the accounting information regarding the transactions in question (direct connection), and within other accounting information from the entity’s accounting system (indirect connection), the conjunction of which can help detect the existence of certain anomalies and possible cases of tax evasion and fraud. To this extent, an example of such a situation would be the unsynchronized dynamic/unusual trend of revenues and expenses or the lack of a certain asset that would justify the necessity of a certain expense that has been entered into the accounting books, etc.

Moreover, the accounting and financial information that emerges from one economic operator can be used in order to detect tax evasion committed by another economic operator, when the information generated by the two informational systems are not consistent, although they concern the same economic transactions carried between the two business partners (in which case there are discrepancies when comparing the data and information).

Therefore, the accounting and financial information that has been manipulated to reflect a certain accounting truth in order to obtain a “targeted” accounting and tax result can be considered both as a clue carrier regarding the existence of tax evasion, and as a means of committing such a crime.

III. ILLUSTRATING THE CAUSES AND EFFECTS OF TAX EVASION USING THE TREE DIAGRAM

As previously stated, the tax literature that overviews the causes that lead to the manifestation of tax evasion is very rich and varied, therefore we have chosen to illustrate, structure and explore, using the tree diagram as a research instrument, some of the key determinants of tax evasion, that are often mentioned in the relevant literature and research studies and articles and possible effects produced by the tax evasion phenomenon. (Fig. 1).

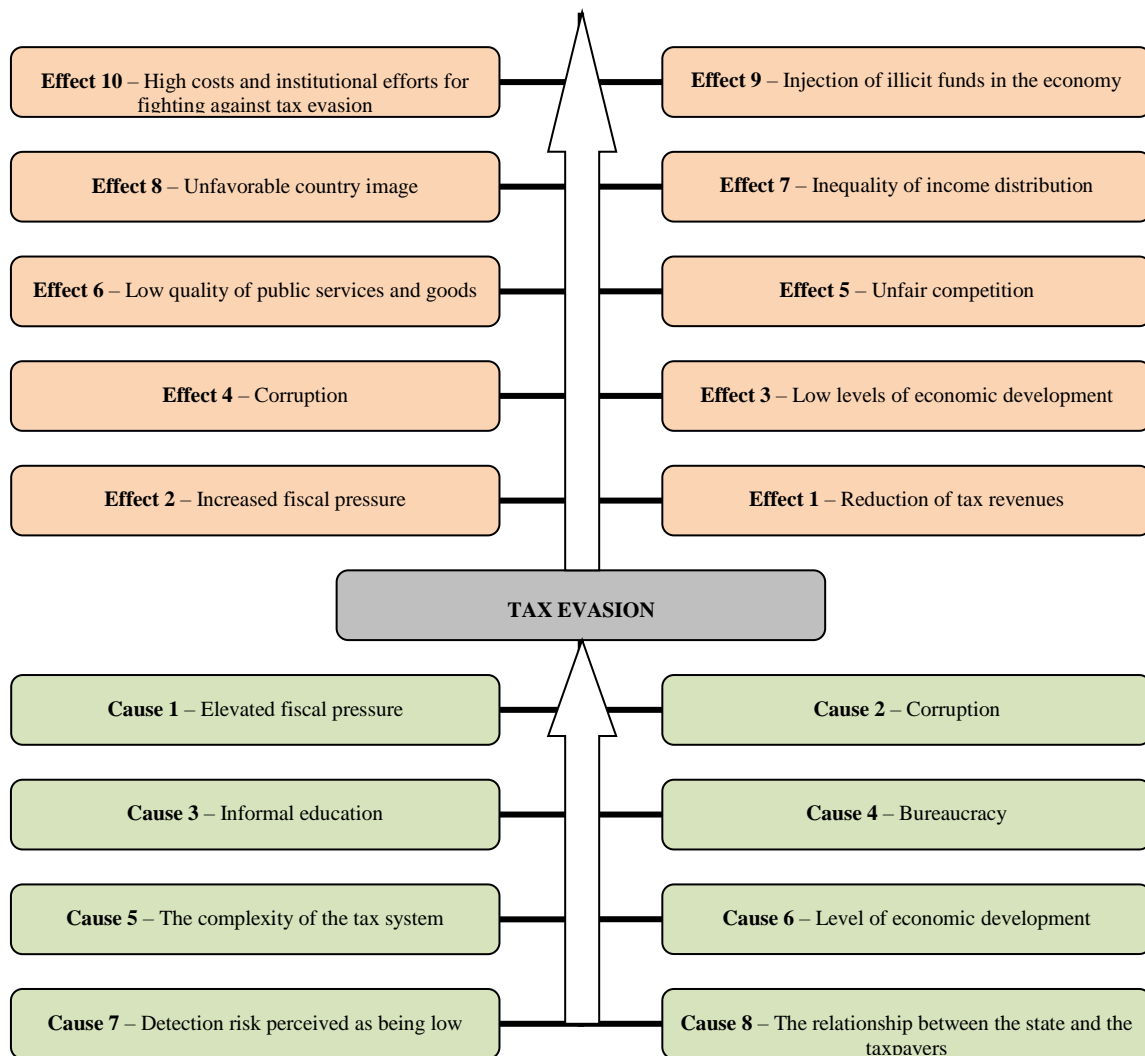


Figure 1 – The tree diagram illustrating the determinants and consequences of tax evasion. Source: own projection

IV. EXPLORING THE DETERMINANTS OF TAX EVASION

▪ Elevated fiscal pressure

The fiscal pressure can be computed both at a state level, as the ratio between the collected tax revenues (including social security contributions) from a certain period of time and the gross domestic product from the same period of time (**Dobrotă, 2011**), and at the level of the economic operators or private persons (under the form of the cost for voluntary tax compliance).

On the one hand, a high fiscal pressure influences the taxpayers' behavior, in the sense that it decreases the voluntary compliance with tax payments due to state budgets and the reporting of income, thus leading to tax evasion. On the other hand, the manifestation of tax evasion, through the harmful effects it produces on the dimension of collected tax revenues, also leads, in order to counterweight such effects, at increased tax rates and thus at an increased fiscal pressure. In this way we are in the presence of a vicious cycle (cause-effect-cause).

▪ Corruption

According to a study (**Buehn and Schneider, 2012**), on the basis of a simulated equations model, there has been established that a large underground economy (shadow economy, that implies the existence of tax evasion) also implies the existence of high corruption levels.

On the one hand, in some opinions (**Braşoveanu, 2010**), there is a negative relationship between corruption and the collection of tax revenues, because: „if those who officially collect tax revenues are involved in corrupt practices (either through public embezzlement or by offering the taxpayer the possibility not to pay taxes in exchange for bribery), then the corruption will directly decrease the volume of collected tax revenues”. On the other hand, corruption spreads its harmful effects on the economy and on the collected tax revenues indirectly also, as it increases the cost of business and decreases the country's attractiveness for potential investors, generating unfair competition among companies carrying out illegal business in the underground economy and those operating on the surface.

Corruption is a determinant for tax evasion, as one resorts to the latter in order to obtain the monetary funds necessary for the illegal payments for obtaining certain unjust advantages, positions, contracts, etc.

As it can be observed, corruption is also an effect of tax evasion manifestation, because usually, the taxpayers that are involved into illegal schemes, in order to reduce the risk of being detected, often corrupt and vitiate the fiscal control systems and not just.

According to some opinions (**Hoanță, 2010**): „the state itself can incite to tax evasion practices, because there is a need for the taxpayers to consume as much as possible. There are two ways through which the state aims at “achieving” tax evasion and those are capital formation and supporting some interest groups.”

▪ Informal education

Another element that can be considered a determinant of the tax evasion phenomenon is, in our opinion, the informal education that a person acquires throughout his or her entire life, outside of the institutions, curricula or educational planned programs (**Coombs and Manzoor, 1974**), on the basis of their daily experiences and of the examples, attitudes and behaviors of those around them (family, friends, colleagues, business partners, etc.).

Therefore, possibly having contact with manifestations of tax evasion in the professional and business areas and possibly observing such a behavior and perceiving it as not entailing any repercussions, can determine a change in the taxpayers' behavior, also taking into account the fact that the taxpayer might perceive a certain unfairness and inequity regarding the whole situation.

▪ Bureaucracy and the complexity of the tax system

Tax evasion can also happen due to certain errors determined by not knowing or wrongfully understanding the laws; it is very difficult to differentiate between the involuntary errors and those made in order to diminish the tax base.

Tax complexity can take many forms, that concern aspects such as – the computation method of tax bases that have to be reported, the complex and numerous legal forms that have to be filled and submitted to tax authorities, the frequent changes of the fiscal laws, the numerous fiscal rules, the multiple possible interpretations of fiscal laws, etc.

Moreover, according to some opinions (**Saw and Sawyer, 2010**), perceiving the fiscal system as a complex one is also due to the fact that the tax legislation is very difficult to read and understand.

▪ The level of economic development

The main conclusions from the research studies carried out regarding the matter (**Schneider, Buehn et al., 2010**) were that underdeveloped countries have a larger underground economy. The impact of the GDP per capita on the underground economy is negative (the higher the GDP per capita is, the more the dimension of the underground economy from that country is dropping), due to the fact that the population from underdeveloped

countries is often involved in illicit practices, such as working without legal forms.

▪ **Detection risk perceived as being low**

A theory from the specialized literature (Sutherland, 1983; Cressey, 1953) regarding the factors that influence people to commit crimes, suggests that there are three elements that determine the manifestation of criminality. Usually this trio can be illustrated as a triangle whose corners are the determinants of engagement in illegal acts: the pressure on the individual, opportunity and rationalization.

In what concerns opportunity, in order to engage into the commitment of tax evasion crimes, it is necessary for the perpetrator to feel that there is a realistic opportunity to use such practices without serious consequences.

Opportunity is related to a person's perception regarding the fact that there is a way of engaging in tax evasion crimes without being noticed or detected. If an individual sees such an opportunity he or she will be more tempted to consider the possibility of initiating illegal actions.

▪ **The relationship between the state and the taxpayers**

(Prado, 2011) presents a general equilibrium model in order to study the interaction between the economic entity's choice to operate in the formal or the informal sector and government policy on taxation and enforcement. The conclusions of the study performed on a sample of 29 countries are that the less strict the enforcement and control of the laws are – together with other determinants of underground economy – higher levels of taxes and stricter enforcement rules – the larger is the size of the informal sector of the economy.

V. CONCLUSION

Tax evasion is not a new or recent phenomenon, however, lately, its alarming and uncontrolled rising (as a phenomenon that cannot be directly quantified) led to considering the measures of fighting against tax evasion and tax fraud as priorities within social and economic policies and strategies both at national and at international levels.

In this context, identifying the determinants of tax evasion that cause the proliferation of this phenomenon is a logic and necessary approach, fundamental in order to counteract the main consequences of tax evasion that can be non-exhaustively listed as follows:

- Reduction of tax revenues,
- Increased fiscal pressure,
- Low levels of economic development;
- Manifestation of corruption;
- Unfair competition in the business environment;
- Low quality of public services and goods provided to the population;
- Inequality of income distribution among members of society;
- Unfavorable country image and lack of attractiveness for possible investors;
- Injection of illicit funds in the economy;
- High costs and institutional efforts necessary for fighting against tax evasion.

The determinants of tax evasion, as they have been identified and explored in this article:

- Elevated fiscal pressure;
- Corruption;
- Informal education;
- Bureaucracy and the complexity of the tax system;
- The level of economic development;
- Detection risk perceived as being low;
- The relationship between the state and the taxpayers, represent a starting point for future empirical

researches that will be done in order to quantify the level of tax evasion and in order to develop a prediction model for the dimension of this phenomenon on the basis of quantifiable indicators (variables) attributed to these determinants of tax evasion.

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