

TAX EVASION AND CORRUPTION – CHALLENGES FOR THE ROMANIAN ECONOMY

MARIAN-ROMEO GUIU

Alexandru Ioan Cuza University of Iasi

Iasi, Romania

guiuromeo@yahoo.com

Abstract

The article aims to highlight the characteristics of some negative phenomena, such as tax evasion and corruption, which affect the economy Romanian. Tax evasion is the most important component of the mechanism of economic-financial crime, and the EU space faces an impressive dynamic of the export and import of economic crime, combating this phenomenon becoming the primary goal of specialized bodies. In this research, the aspects, concepts and causes of these negative phenomena will be analyzed, as well as the interdependence between them and the fiscal pressure. Also, analyzing the level of tax collection in Romania compared to the other EU states, is useful to highlight the existence of an interdependence link between a high level of taxation (which has the effect of increasing the fiscal pressure on taxpayers) and the increase of the level of tax evasion. Further research will also focus on the analysis of the impact that the increases in taxes and fees will have on the degree of payment compliance on the part of taxpayers.

Keywords: *tax evasion; corruption; fiscal pressure.*

JEL Classification: H21, H26, H30.

1. INTRODUCTION

Although from the perspective of scientific research, the concept of tax evasion has given rise to numerous analyzes both from the perspective of the fiscal or legal field, the definitions of this concept have not always been eloquent, the approach being carried out in a unilateral, contradictory way and that launched hypotheses more or less precise but lacking realistic and achievable objectives. Tax fraud and tax evasion is a serious and complex problem that requires a coordinated approach at national, European and international level. The economic and financial crisis has generated many problems for most European governments, which have tried to adopt viable measures to ensure that they can keep public spending under control, ensure a more efficient collection of budget revenues and reduce the phenomenon of tax evasion and fraud, in such a way that economic growth can be achieved. It is very important to study the evolution and behavior of tax evasion, in order to find quick solutions to reduce this phenomenon.

2. ASPECTS FROM THE SPECIALIZED LITERATURE IN THE FIELD OF TAX EVASION AND CORRUPTION

In the specialized economic literature, the analyzed problem is the subject of scientific studies by various economists, teaching staff, scholars, and more recently also students, considering the history of the phenomenon of evasion and fraud fiscal in the context of increasing the budget deficit caused largely by the level of collection of taxes owed by taxpayers.

In theory, it is known that tax evasion can be seen as a phenomenon with two main actors, on the one hand, the taxpayer - lacking a financial education, who tries to evade paying the established taxes and fees, in order to achieve some advantages of an immediate material nature, and on the other hand - the state that seeks through various instruments to prevent a reduction in tax payments to the consolidated budget. While some studies of specialized literature such as those of (Dinga, 2008), claimed that tax evasion is not a specific component of the underground economy as it involves legal activities not reported to the authorities, and in this context it would be much more appropriate that evasion tax to be located in the border area between the underground economy and the official economy, other studies such as (Olabisi, 2010) state about tax evasion as an intentional practice of economic agents not to report the real values to the authorities, in order to be able to reduce the obligation fiscal, although this method involves certain illegal actions from a fiscal point of view.

Instead, the study carried out by (Schneider and Klingmair, 2004) highlighted the fact that between the underground economy and tax evasion there is a link of interdependence, and the condemnation of the activities that make up the underground economy through effective legislative measures will be felt in full, contributing to the reduction of the phenomenon of evasion fiscal.

In the specialized literature, there are other studies that empirically address the interdependence between tax pressure and tax evasion (Amarița, 2017), following the study, identified several causes underlying tax evasion, considering that the excess of tax burdens and the insufficiency of citizens' education determine the extent of tax evasion. Under this aspect, he considered that the efficiency of a tax system consists in the degree of tax consent and that an insufficient education of citizens also has effects on the increase of the phenomenon of tax evasion and concluded that the lack of control carried out by qualified personnel and the gaps of the tax legislation can determine the amplification of the effect of tax evasion and that a decrease in the tax pressure on taxpayers would lead to the decrease of tax evasion, launching a solution in this sense, the best way to achieve the objectives is to create structures that adapt to the changes from the market, to be based on low taxes and to be charged at an extended level of taxation. Gyuricza *et al.* (2017), following the study, they came to the conclusion that the spirit of tax evasion is born from the simple

game of interest, they argued that, whatever the tax rate charged, man, by his nature, always tends to put the general interest behind to the private, as he is inclined to regard the tax as more of a detriment than a legitimate contribution to the public expenditure, and to always look with evil eyes on him who wants to diminish his patrimony, drawing attention to the fact that it is known that some taxpayers will seek the kind of ingenious methods to reduce the amount of tax obligations.

While in the study carried out on the Romanian economy concluded that, the main reason why the revenue/GDP ratio is relatively low in Romania is tax compliance (Sudharshan *et al.*, 2012), in addition, the tax base is so narrow and there are numerous tax exemptions, so that the receipts represent only a small part of the theoretical maximum collection considering the statutory tax. (Keynes,1997), was a supporter of the idea that, if the state reduced its taxes, it would cause an increase in the consumption rate of individuals, a relaxation of business processes and an increase in the demand for ordinary goods. He stated that, the level of a contribution consisting of fees and taxes must be correlated with the level of wealth and income, otherwise tax evasion would occur, also launching a solution in this regard, namely the introduction of a substantial tax on transfers, which would have been applied to all transactions to combat the speculation of the entrepreneurial spirit.

(Durovic *et al.*, 2019) concluded that reducing the number of taxes to be paid encourages economic growth, while a decrease in the level of taxes contributes to and increases the level of economic activity, but in terms of fiscal effects, research results are somewhat contradictory, as stated that the impact of state taxes could be both positive and negative on the economy of the respective country (Pjesky, 2006).

We all know that the Gross Domestic Product is the performance indicator of a state's economy, in this sense at the level of the European Union, (Mutaşcu *et al.* 2007) researched the impact of direct and indirect taxes on gross domestic product for the period between 1995 and 2005 and concluded that, for a 1% increase in direct taxes, GDP per capita will increase by 1.61%, and in the case of indirect taxes, an increase of 1% will cause GDP per capita to decrease by 0.83%, suggesting the idea that, the process of fiscal harmonization would be more appropriate instead of competition.

Other authors believed, at the basis of this phenomenon, lies the incorrect and incomplete management of records regarding the determination of income, expenses, and tax obligations, nothing could be truer, but no analysis was made of the causes that led a taxpayer to avoids declaring, highlighting and paying tax obligations. It is known that the evasions phenomenon cannot be eradicated if you do not make a correct diagnosis and evaluation of it and do not have the necessary levers to combat it at hand. Because why not, we must recognize that as long as there is an obligation to pay, there is also the temptation to evade

payment, therefore, any of the procedures for evading the payment of tax obligations are based on multiple causes, which can be identified and kept under control by the state. While other authors had a more realistic approach to the concept of tax evasion, starting from the idea that the reality of a healthy economic system derives from the very principle of contribution, so if we choose to live in a community, it is necessary to contribute each in part to its proper functioning, because inevitably, the state must regulate a fiscal system, the purpose of which is to ensure the revenues necessary for the optimal functioning of state institutions and authorities.

Regarding corruption, in the specialized literature for a longtime researchers considered corruption as a predominantly political and cultural phenomenon and its removal impossible to achieve (Tudorel *et al.*, 2008). Specialized studies have highlighted the fact that this negative phenomenon is present in all countries, both developed and less developed, but each country has a specific corruption potential, but its extent is influenced by the country's general fiscal structure and fiscal management systems (Vasquez *et al.*, 2006). Also, the integrity of civil servants is an important factor in combating tax evasion, if the corrupt civil servants find during a specialized check the existence of an illegal act with the consequence of depriving the budget of the statute of collecting some income from fees and taxes and decide to cooperate with these taxpayers in the exchange of bribes, then corruption becomes a serious problem for the institution that manages the finances of a country if no measures are taken to combat it.

Through the prism of the arguments listed above, in the context of the accentuation of the budget deficit caused to a large extent by the degree of collection of taxes owed by taxpayers, we consider current research, its approach requiring a documentation based on the knowledge accumulated in a practical way, corroborated with a perseverance in researching from a fiscal, accounting, legislative point of view, the causes that influence this phenomenon in relation to the surrounding reality.

3. RESEARCH METHODOLOGY

The present research was carried out in an area where, from an academic point of view, there are not many recent studies, and combating these phenomena, over time, became the primary goal of the specialized bodies that imposed themselves by developing policies fiscal adapted to the dynamics recorded by tax evasion and corruption, through which to combat their weight in society through effective measures.

The research started from analyzing the share of budget losses due to the phenomenon of fiscal evasion. In this sense, we collected information by consulting the statistics provided by Eurostat regarding the value of GDP and tax revenues as a percentage of this indicator, for each of the 28 EU member states

in 2021. We also added the CPI variable that reflects the index of the perception of corruption taken from the Transparency International statistics, respectively the level of taxation taken from the reports of the World Bank in order to establish the various connections and correlations between the dimension of tax evasion and the level of taxation. It is known that the tax pressure is fully felt by the tax and tax payers, so an honest, honest taxpayer voluntarily agrees to pay tax obligations, but the problem arises when the level of taxes and fees reach the limit of bearability, a fact that causes that taxpayer to change his behavior, being "obliged" to resist the competitive economic environment, to look for different methods of evading the payment of taxes and fees.

This behavior was best captured (Laffer, 1980), starting from an idea experimented by the famous Adam Smith, graphically translated the so-called Laffer curve, according to which tax rates that are too high destroy the basis on which taxation acts, respectively, the income resulting from taxation increases more sharply at low levels of taxation. The concept of the Laffer curve was first mentioned by Jude Wanniski, who in 1974 published an article in *The Public Interest*, entitled *Taxes, Revenues, and the Laffer Curve*.

4. RESULTS

According to the data highlighted in Table 1, it follows that the countries in the EU that register the highest level of tax evasion are Greece, Italy and Romania. If we analyze the data we can conclude that there is a close interdependence between the level of tax evasion and the corruption perception index, it can be seen that in the countries that register a low level of the CPI (Austria, Denmark, Estonia, the Netherlands, Germany, Sweden, Luxembourg) the share of tax evasion in GDP is lower, while in countries where the corruption perception index registers a high level and the share of tax evasion in GDP shows a high share.

Regarding the correlation between the average level of taxation and the CPI index, it should be mentioned that the study highlighted the fact that in some countries, such as Ireland, Luxembourg, Denmark, which register a level of taxation below the EU average, the CPI index shows us a system that tends to be as least corrupt, in time that in other countries such as Austria, Belgium, the Netherlands, Sweden, although they register a level of taxation above the average of the EU states, the CPI index shows us a system that tends to be as least corrupt.

In our opinion this shows that a high level of taxation it does not always imply a high level of corruption and that other factors must be introduced into the relationship, which can influence the behavior of the taxpayer.

Table 1. Variables subject to analysis

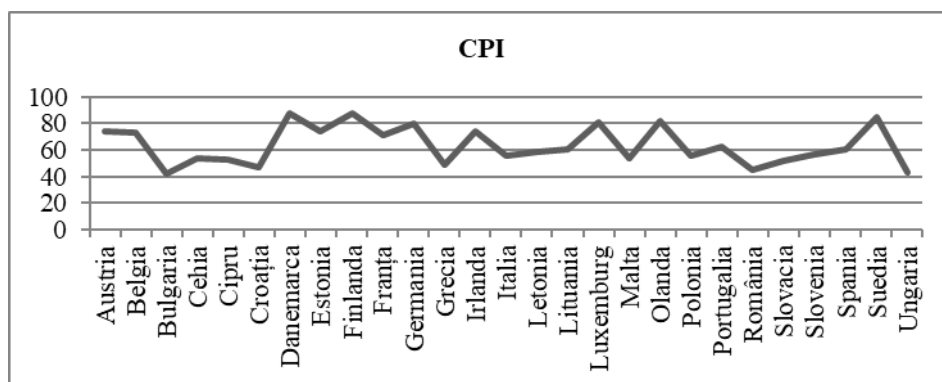
Country	Share of tax evasion in relation to GDP (%)	Average level of taxation	IPC 0-100, where 0 is very corrupt, 100-not corrupt	Tax revenues (% of GDP)
Austria	3.81	53.00	74	44.53
Belgium	7.42	57.00	73	44.35
Bulgaria	8.43	27.1	42	31.40
Croatia	7.97	19.00	47	36.15
Cyprus	9.13	23.21	53	35.99
Czechia	5.31	48.52	54	34.90
Denmark	6.29	26.10	88	48.80
Estonia	6.81	49.40	74	34.90
Finland	5.18	40.10	88	42.93
France	5.41	66.50	71	47.70
Germany	4.18	48.80	80	43.88
Greece	11.31	49.90	49	40.30
Hungary	8.32	48.00	43	33.60
Ireland	2.71	25.95	74	22.54
Italy	11.48	65.41	56	43.50
Letonia	7.12	35.00	59	33.80
Lithuania	8.39	42.70	61	31.45
Luxembourg	3.19	20.30	81	38.90
Malta	9.51	41.80	54	32.50
Netherlands	3.35	39.00	82	38.85
Poland	8.28	38.80	56	37.60
Portugal	6.70	42.54	62	37.45
Romania	10.27	43.80	45	27.20
Slovakia	6.91	48.70	52	35.12
Slovenia	6.90	32.00	57	37.90
Spain	5.68	58.30	61	42.93
Sweden	3.81	49.45	85	44.60

Source: author's works (Eurostat-Fiscal revenues include CAS)

Regarding the relationship between the level of tax evasion and the level of taxation, it can be stated that in principle there is a link between the two variables, in the sense that a high level of taxation also corresponds to a high share of the weight of tax evasion in GDP, with the exception of some countries such as France, Spain, Sweden, Germany which, although they record a high level of taxation, the degree of tax evasion is still low, which leads us to the idea that when analyzing the phenomenon of tax evasion, we must also take into account other criteria of a cultural nature, geographical, respectively the level of financial education of taxpayers. Regarding the collection of taxes in Romania

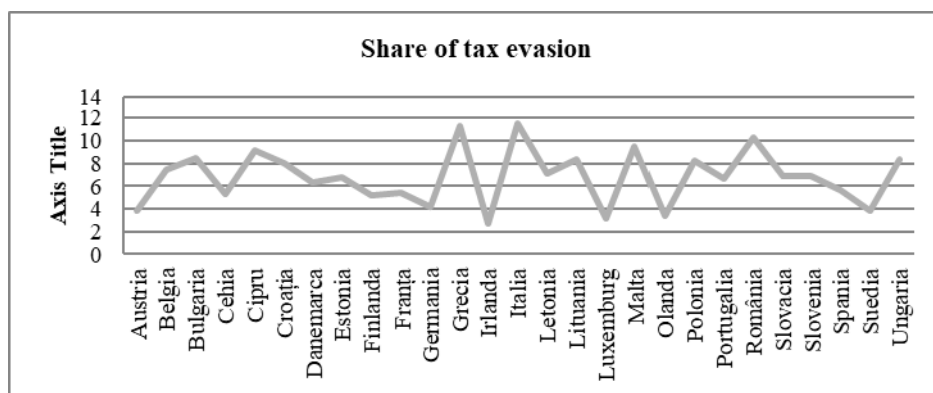
compared to the other EU states, according to the Annual Report prepared by the Fiscal Council, a low level of the share of budget revenues in GDP was also recorded in 2021, respectively of 32.8%, resulting in a gap of 14.1 pp compared to the European average of 46.9%, Romania being followed only by Ireland compared to EU member states.

In Figures 1 to 3, the evolution of the 3 analyzed indicators CPI, Weight of evasion tax revenues from GDP, respectively the share of tax revenues in relation to GDP.



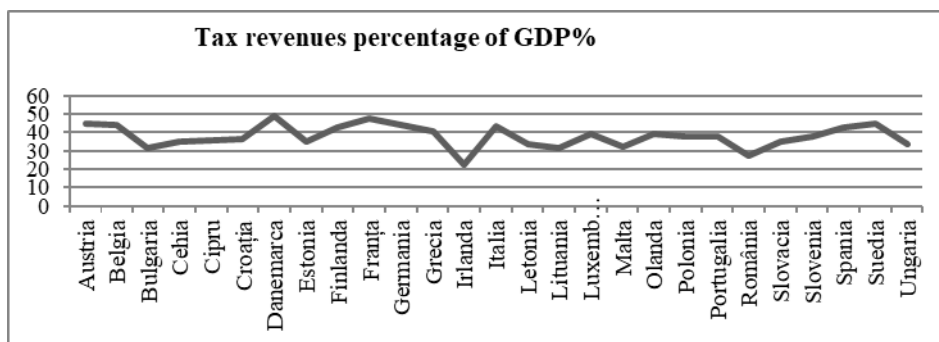
Source: author's work

Figure 1. Corruption perception index at the level of EU countries



Source: author's work

Figure 2. The share of tax evasion in relation to GDP



Source: author's work

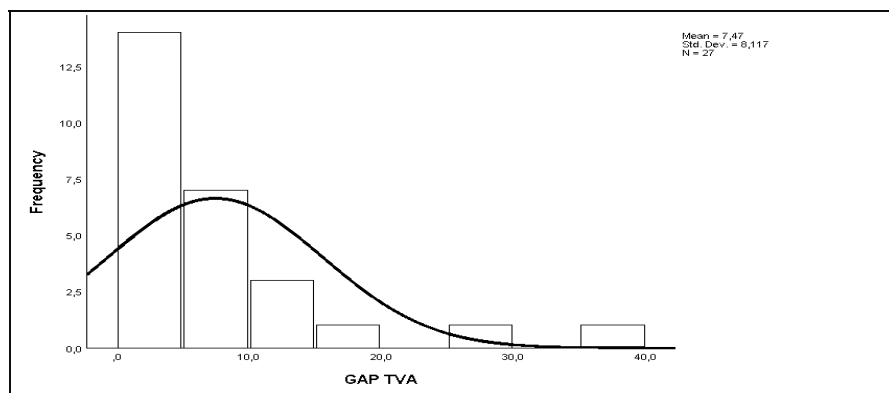
Figure 3. Share of tax revenues in relation to GDP

The level of fiscal revenues composed of taxes and social contributions reached 27.2% of GDP in 2021, Romania still being in the penultimate place, with a gap of 14 pp compared to the EU average (41.2% of GDP). Therefore, if we analyze the evolution of these indicators compared to the previous year (2020), we find that the gap that separates Romania from the EU28 average has deepened both in the case of fiscal revenues by 0.2 pp, and in the case of budget revenues by 0.6 pp. as regards the share of tax revenues in GDP recorded by Romania in 2021, it is significantly below that of other countries with similar economies, such as Slovenia (37.9%), Poland (37.6%), the Czech Republic (34.9%) and Hungary (33.6%). Compared to Bulgaria, the share of budget revenues in GDP is lower by 6.2 pp, and that of tax revenues by 4.6 pp. If we refer to the structure of tax revenues in Romania, the share of receipts from indirect taxes in 2021 was of 39.3% being higher than the European average which reflects a percentage of 33%, but below the level recorded by countries such as: Hungary 52.1%, Bulgaria 50.6%, Poland 40.4%.

Regarding the share of insurance contributions social sector in tax revenues reached a level of 41.9% in 2021, occupying the fourth position after countries such as the Czech Republic 47.6%, Slovakia 44.8% and Slovenia 44.3%. The same situation was not the case direct taxes, where Romania registers one of the lowest shares in tax revenues in the EU, namely 18.8% compared to the EU average, 32.3%.

The structure of budget revenues in Romania is predominantly oriented towards indirect taxes and revenues from social contributions (together they represent 82.6% of tax revenues, the highest value in the EU), while, at the European level, there is a tendency to balance the weight direct taxes, indirect taxes and social security contributions (respectively, an EU average of 32.3%, 33% and 34.7%). If we continue with a brief analysis of the level of VAT collection in Romania (the main source of fiscal budget revenue), in nominal

terms, we can say that in 2021 our country collected 15.511 billion euros from the VAT budget in 2021, compared to expected revenues of 24.5 billion euros, resulting in a deficit of 8.996 billion euros, thus our country recorded the third largest VAT compliance gap in the EU, after Italy (-14.6 billion euros) and France (-9.5 billion euros). In Figure 4 we have presented the evolution of the VAT Gap in the 27 member states of the European Union.



Source: own processing based on data provided by Eurostat

Figure 4. Evolution of the VAT Gap, European Union, 2021

Analyzing the data in Table 2, we can see that the average value recorded by the dependent variable for the year 2021 in the member states of the European Union is 7.467, with a variation that starts from 0.2 and reaches 36.7. We can also observe that the value of the Skewness asymmetry coefficient is 2.385, reflecting the fact that the distribution is skewed to the right which means that a positive skewness.

Table 2. Descriptive statistics of the variable – VAT Gap

	Descriptive Statistics											
	N Statistic	Range Statistic	Minimum Statistic	Maximum Statistic	Mean Statistic	Std. Error Std. Error	Std. Deviation Statistic	Variance Statistic	Skewness Statistic	Std. Error Std. Error	Kurtosis Statistic	Std. Error Std. Error
GAP TVA	27	36,5	,2	36,7	7,467	1,5620	8,1166	65,880	2,385	,448	6,284	,872
Valid N (listwise)	27											

Source: author's work

The approach to tax evasion must also be reanalyzed from the perspective of human behavior, as studies have shown that this phenomenon, which derives from the individual's mode of action, is not devoid of rationality, and with the rapid increase in taxes, there is a considerable increase in this phenomenon, in this sense, we intend that through a future study we will analyze the evolution of the phenomenon of tax evasion for a period of 15 years, after which we will obtain results that will allow us to make a prediction regarding the evolution of

this negative phenomenon. Regardless of its size, tax evasion is a negative phenomenon, and failure to achieve the collection program from the perspective of tax revenues can have a significant impact on the budget deficit. In the context of failure to achieve the collection program, the following effects may occur:

- Increase in the budget deficit, so the government must cover expenses with available resources, including through loans or by reducing other expenses;
- Pressures on public finances, decision-makers will have to find other sources of financing to cover the resulting deficit, and this may lead to concerns about the sustainability of public debt and may affect the country's credit ratings;
- Reduction of investment capacity;
- It affects the national economic stability;
- It can lead to the emergence of social and economic inequities;
- It affects the purchasing power of the national currency.

5. CONCLUSIONS

Tax fraud and tax evasion represent a serious and complex problem that requires a coordinated approach at national, European and international level. The economic and financial crisis has generated many problems for most European governments, which have tried to adopt viable measures to ensure that they can keep public spending under control, ensure a more efficient collection of budget revenues and reduce the phenomenon of tax evasion and fraud, in such a way that economic growth can be achieved. Following the study undertaken, we can appreciate that between the level of tax evasion and the corruption perception index there is a close link of interdependence, thus we identified that countries such as (Austria, Denmark, Estonia, Holland, Germany, Sweden) which register a low level of the CPI, the share of tax evasion in GDP is lower, while in countries where the corruption perception index registers a high level (Romania, Greece, Hungary, Malta, Cyprus, Bulgaria) and the share of tax evasion in GDP presents a share raised. Also, a high level of taxation, which has the effect of increasing the fiscal pressure on taxpayers, causes an increase in the level of tax evasion.

Since ANAF has the central role in the administration of the collection of taxes and duties and holds all the levers to reduce the "motivation" of taxpayers to avoid paying tax obligations in order to increase the degree of voluntary compliance with the payment of duties and taxes owed to the state budget, we believe that a reform of this institution is required. Thus, the ANAF reform through digitization provided for in the PNRR aims to increase the revenue/GDP ratio by:

- reducing the fiscal gap to VAT;
- efficient administration of taxes and fees;
- increasing the degree of voluntary compliance on the part of taxpayers when paying fees and taxes;
- decreasing corruption among fiscal structures with fiscal verification duties.

In conclusion, achieving fiscal objectives by increasing the quality of services, implementing integrated digital solutions, as well as increasing institutional efficiency and transparency, followed by an upward trending collection level, can contribute to reducing the phenomenon of tax evasion.

References

- 1) Amarița A. (2017). Fiscal evasion in Romania. *Journal of Statistics – Supplement*, 1, pp. 3-21.
- 2) Dinga, E. (2008). Theoretical considerations on tax evasion and fraud. *Financial Studies*, 4, pp. 20-50.
- 3) Durovic, T.J., Milenkovic, I. and Kalas B. (2019). The relationship between direct taxes and economic growth in OECD countries. *Teme economice*, 57(3), pp. 273-286.
- 4) Gyuricza, S.I. (2017). Conceptual aspects of tax fraud. *Expertiza și Auditul afacerilor*, 4, pp.18-23.
- 5) Keynes, J.M. (1997). *General Theory of Employment, Interest and Money Reprinted Edition*. London: Prometheus Books UK, pp. 219-287.
- 6) Lafer, A. (1980). *The Laffer Curve: Paste, Present, and Future*. Washington DC:,The Heritage Foundation , pp. 1-16.
- 7) Martinez-Vasquez, J., Arze, X. and Boex, J. (2006). *Corruption, fiscal policy and fiscal management*. Bingley: Emerald Group Publishing Limited, pp. 1-10.
- 8) Mutașcu, M.I., Crasneac, A.O. and Dănuțiu, D.C (2007). The impact of taxes on economic growth EU case. *MPRA Paper*, 6143, pp. 19-25.
- 9) Olabisi, J. (2010). An assessment of tax evasion and tax avoidance in Lagos, Nigeria. *Journal of Research in National Development*, 8(1). pp. 17-27.
- 10) Pjesky, R. (2006). What do we know about taxes and state economic development? A replication and extension of five key studies. *Journal of Economic Insight*, 32(1), pp. 25-40.
- 11) Schneider, F. and Klinglmaier, R. (2004). Shadow economies around the world: What do we know? *Universitat Linz Working paper*, 403, pp. 20-63.
- 12) Sudharshan, C. (2012). The Challenges to Long Run Fiscal Sustainability in Romania. *Policy Research Working Paper*, 5927, pp. 37-51.
- 13) Tudorel, A., Ani Matei, I. and Roșca, Gh. (2009). *Corruption. An economic and social analysis*. București: The Economica Publ. House, pp 14-17.