

**EVOLUTION OF TAX EVASION AND THE UNDERGROUND ECONOMY AT
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domnicapopovici98@yahoo.com***Ec. Mihaela – Ionela SOCOLIUC***stanciuc_mihaela@yahoo.com***Abstract**

One of the main causes of the production of economic problems is the vastness of these phenomena, being encountered in most countries regardless of their level of development. Because they are not characteristic phenomena only to the contemporary world, they exist for all time, the limitation of the adverse consequences induced by them is sought, the elimination being practically impossible. The paper aims to show the characteristics of these phenomena that have a negative impact, both for Romania and for the other states. The data needed for the analysis are up-to-date and capture the characteristics of our country in relation to the other EU Member States. The research is quantitative, its purpose and role being to identify the level of tax evasion and the underground economy on the two plans (international and national). The main objective of the paper is to reflect the level, dynamics and evolution of tax evasion, as well as to determine the size of the unofficial economy, both in Romania and internationally. The research methodology involves conducting a study that involves identifying the level and evolution of tax evasion and the underground economy. The main result of the analysis is represented by the fact that the evolution of the two phenomena is alarming and that all the Member States are trying to diminish them and the effects they have on the whole economy.

Key words: *fraud; international level; national level; tax evasion; underground economy.*

JEL Classification: *M40.*

I. INTRODUCTION

In Romania, through the multitude of manifestations, in recent years, these have been in a continuous growth and expansion, affecting more and more the development of the economy and fueling inequalities.

Through the numerous forms of manifestation and the multitude of effects it produces, tax evasion has direct repercussions on the level of tax receipts and revenues, leads to distortions in the market mechanism and can contribute to the "support" of the taxpayers in identifying optimization solutions, more or less legal, of the tax burdens they are subjected to, the taxation being approached by them as a "illegitimate confiscation" of their income (Popoiu, 2015: 1).

The measures taken at national level are important, but they cannot manage to combat the evasion phenomenon and increase the level of the underground economy alone (Socoliuc, Mihalciuc & Cosmulese, 2018). These must be combined with the legal means found at European and international level to alleviate problems.

It is considered that joint actions at European level are more effective, and are intended to encourage third countries to apply minimum standards of good governance in terms of taxation.

II. AT THE INTERNATIONAL LEVEL**II.1. TAX EVASION**

International tax evasion is encouraged by the existence of small legal entities with special status or of state type, known in the specialized literature under the name of "tax havens" or "tax breaks". Tax havens are also known as "tax-free zones".

Fiscal paradise is "a generic term that defines a state, a country or a territory that practices low or even zero taxes, while providing stable legislation, good economic conditions and a low rate of corruption, including for sources of income. foreign, respectively, a country that encourages by its fiscal policy the exercise in its territory of certain specific economic activities" (www.wikipedia.ro).

The moment that marks the rise of the importance of tax havens is the end of World War II.

We believe that these advantages of tax havens increase the reluctance and inappropriate behavior of taxpayers when it comes to paying tax obligations.

Tax havens can be classified into two broad categories (see Figure 1), namely (Mecşa, 2016: 12):

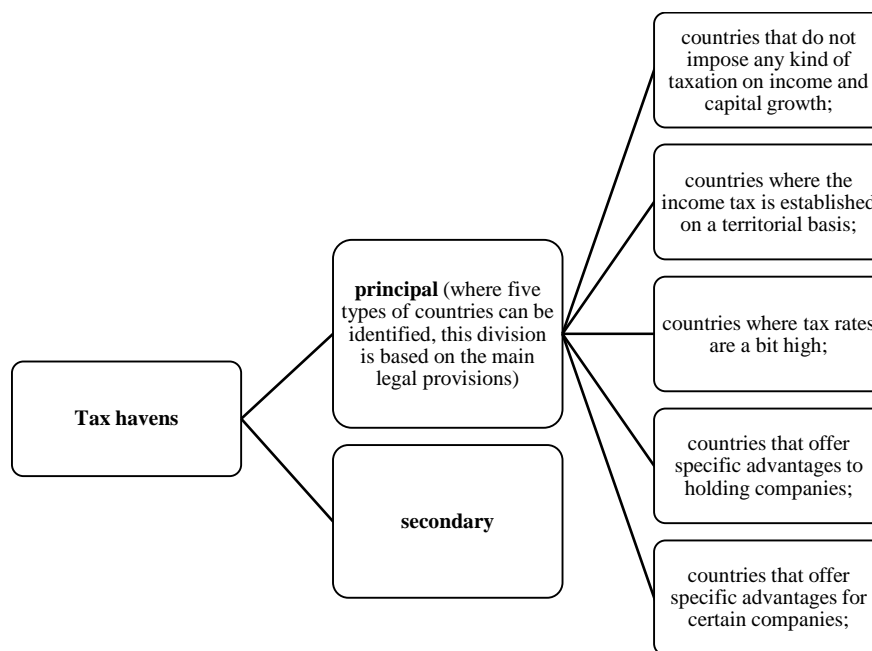


Figure 1 – Classification of tax havens

Source: Author's own processing

These tax havens encourage the increase of the level of tax evasion and fraud by the fact that they are not fulfilled and the tax obligations are not respected.

A study on tax evasion by the Group of the Progressive Alliance of Socialists and Democrats at the University of London found that "although the volume of taxes avoided in the EU has decreased by 12% to 16% since 2009, it is still very high."

According to the study, in the last year EU countries have lost about 824 billion euros in taxes. This is far more than the amount the public sector misses (50 to 190 billion euros), according to tax expert Richard Murphy, who conducted the study.

The data presented in the following table (see Table 1) represents the best estimate of the cost of tax evasion in the 28 Member States of - "the amount could be between 750 and 900 billion euro throughout the EU", said Murphy.

Table 1. The cost of tax evasion in the Member States of the European Union

The Country	Value (Bilion Euro)
Austria	12,9
Belgium	30,4
Bulgaria	3,8
Cyprus	1,6
Czech Republic	8,8
Croatia	3,5
Denmark	17,5
Estonia	1,4
Finland	10,7
France	117,9
Germany	125,1
Greece	19,9
Hungary	9,1
Ireland	6,9
Italy	190,9
Latvia	1,7
Lithuania	3,1
Luxembourg	1,6
Malta	0,9
Netherlands	22,2
Poland	34,6
Portugal	11

The Country	Value (Billion Euro)
Romania	16,2
Slovakia	5,4
Slovenia	2,6
Spain	60
Sweden	16,9
United Kingdom	87,5
TOTAL	824,1

Source: Author's own processing after: Armstrong, 2019

Analyzing the data in this table, we find that no matter how the "crime" of tax evasion was committed (by "circumventing" the law respectively by false declarations of results), it costs billions of euros the EU states and beyond. Among these states, there is Romania, which, in our opinion, also presents, following the amount shown above, an alarming and increasing number of the cost of evasion.

It is noted that the value of 190,9 billion euros is the highest and belongs to Italy, the next top places being occupied by Germany (with 125,1 billion), France (with 117,9 billion) and the United Kingdom (with 87,5 billions).

Thus, it is noted that in the developed countries the highest rates of evasion were registered due to the influence that, in our opinion, the increase of the tax pressure on the taxpayers.

In the other extreme is Malta with 0,9 billion, Estonia with 1,4 billion, Luxembourg and Cyprus with 1,6 billion.

In this study, Romania is among the top 10 countries whose costs exceed 15 billion euros. It is one of the developing states where, we believe, the law is permissible by admitting the circumvention, non-fulfillment and interpretation at will, thus realizing the evasion phenomenon, namely tax fraud.

It is observed that the economic development of the states has an impact on the increase of the evasion and the more the states "enrich" the more the evasion develops.

II.2. THE UNDERGROUND ECONOMY

The presence of an underground economy could cause significant losses to government revenues and could also be a serious breach of labor regulations.

We find that local financial development is associated with a smaller size of the underground economy, controlling the endogenous potential of financial development and other determinants of the underground economy (Capasso & Jappelli, 2013: 167-178).

The underground economy "exists in all countries of the world, in different proportions in GDP. Underground economy appears in the specialty literature under various names (over 20): occult economy, hidden, disguised, parallel, annex, dangerous, ghost, invisible, unofficial, dual, cash, informal, secondary, illegal, shadow, unmeasured, counter-economy" (Braşoveanu, 2010: 68-80).

The underground economy is defined as "legal economic activity, but hidden by public authorities to avoid paying taxes and social contributions or to avoid complying with legal standards on the labor market and other administrative procedures" (www.conso.ro).

According to the literature there are three types of causes that produce and influence this phenomenon (see Figure 2):

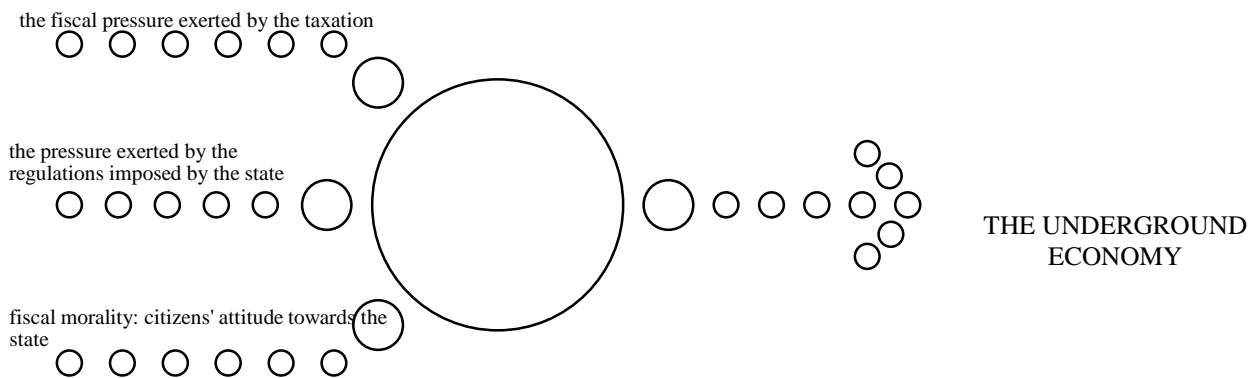


Figure 2 – The main causes that produce the evolution of the underground economy

Source: Author's own processing after: Braşoveanu, 2010: 68-80

In the Table 2 and Graph 1 we will present the level and evolution of the underground economy expressed as a percentage of GDP in all EU Member States.

Table 2. Underground economy expressed as a percentage of GDP for the 28 EU Member States, from 2006-2017

The Country	The year											
	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
Austria	9,7	9,4	8,1	8,5	8,2	7,9	7,6	7,5	7,8	8,2	8,93	7,1
Belgium	19,2	18,3	17,5	17,8	17,4	17,1	16,8	16,4	16,1	16,2	17,8	15,6
Bulgaria	34	32,7	32,1	32,5	32,6	32,3	31,9	31,2	31	30,6	29,17	29,6
Cyprus	27,9	26,5	26	26,5	26,2	26	25,6	25,2	25,7	24,8	23,3	23,6
Czech Republic	18,1	17	16,6	16,9	16,7	16,4	16	15,5	15,3	15,1	14,83	14,1
Croatia	31,2	30,4	29,6	30,1	29,8	29,5	29	28,4	28	27,7	22,96	26,1
Denmark	15,4	14,8	13,9	14,3	14	13,8	13,4	13	12,8	12	14,70	10,9
Estonia	29,6	29,5	29	29,6	29,3	28,6	28,2	27,6	27,1	26,2	23,8	24,6
Finland	15,3	14,5	13,8	14,2	14	13,7	13,3	13	12,9	12,4	13,3	11,5
France	12,4	11,8	11,1	11,6	11,3	11	10,8	9,9	10,8	12,3	11,65	12,8
Germany	15	14,7	14,2	14,6	13,9	13,2	12,9	12,4	12,2	12,2	11,97	10,4
Greece	26,2	25,1	24,3	25	25,4	24,3	24	23,6	23,3	22,4	26,45	21,5
Hungary	24,4	23,7	23	23,5	23,3	22,8	22,5	22,1	21,6	27,9	25,23	22,4
Ireland	13,4	12,7	12,2	13,1	13	12,8	12,7	12,2	11,8	11,3	13,89	10,4
Italy	23,2	22,3	21,4	22	21,8	21,2	21,6	21,1	20,8	20,6	22,97	19,8
Latvia	29	27,5	26,5	27,1	27,3	26,5	26,1	25,5	24,7	23,6	22,23	21,3
Lithuania	30,6	29,7	29,1	29,6	29,7	29	28,5	28	27,1	25,8	25,15	23,8
Luxembourg	10	9,4	8,5	8,8	8,4	8,2	8,2	8	8,1	8,3	10,38	8,2
Malta	27,2	26,4	25,8	25,9	25,4	25	24,4	23,8	23,5	23,3	29,43	23,6
Netherlands	10,9	10,1	9,6	10,2	10	9,8	9,5	9,1	9,2	9	10,77	8,4
Poland	26,8	26	25,3	25,9	25,4	25	24,4	23,8	23,5	23,3	25,1	22,2
Portugal	20,1	19,2	18,7	19,5	19,2	19,4	19,4	19	18,7	17,6	17,82	16,6
Romania	31,4	30,2	29,4	29,4	29,8	29,6	29,1	28,4	28,1	28	25,94	26,3
Slovakia	17,3	16,8	16	16,8	16,4	16	15,5	15	14,6	14,1	15,33	13,0
Slovenia	25,8	24,7	24	24,6	24,3	24,1	23,6	23,1	23,5	23,3	24,09	22,4
Spain	20,2	19,3	18,4	19,5	19,4	19,2	19,2	18,6	18,5	18,2	22,01	17,2
Sweden	16,2	15,6	14,9	15,4	15	14,7	14,3	13,9	13,6	13,2	13,28	12,1
United Kingdom	11,1	10,6	10,1	10,9	10,7	10,5	10,1	9,7	9,6	9,4	8,32	9,4
The average of the 28 European states	21,1	20,3	19,6	20,1	19,9	19,6	19,3	18,8	18,6	18,3	17,8	17,1

Source: Author's own processing after: Olteanu & Pascu, 2017: 277

The main negative effect that a large size of the underground economy can have is the diminution and decrease of the growth rate of the official economy.

The statistics related to the phenomenon, regarding Romania and the other EU states are worrying and the negative effects of the growth of the level of the underground economy have a strong impact and are felt both at the level of the GDP and at the level of the tax receipts.

Analyzing the data from the table we see that the highest values are found in Bulgaria, Romania and Croatia, these states have the size of the underground economy above the European average every year of the analysis.

In 2017, the values found in these states are increasing. Bulgaria has a value of 29,6%, an increase of 0,43%; the value declared in Romania increases in 2017 compared to 2016 with about 0,36% registering a value of 26,3%, and Croatia has an increasing value in 2017 with 3,14% (the value in 2016 was 26,1%).

At the opposite pole are Austria and Luxembourg with the lowest values; Austria with 7,1% and Luxembourg with 8,2%. Both values are on the rise. The values for the years 2006-2015 are oscillatory.

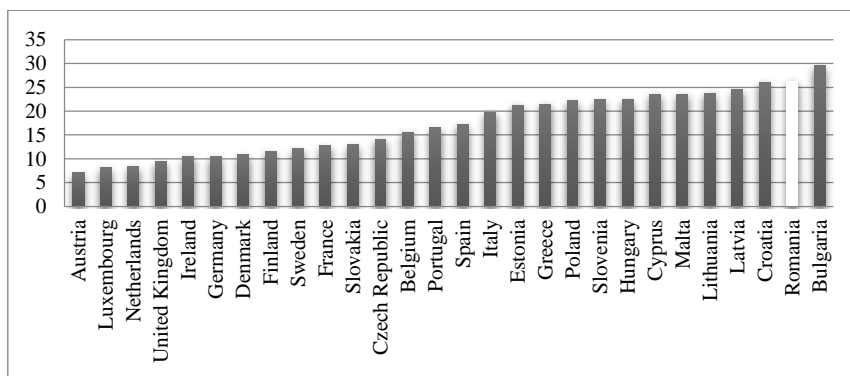


Figure 1 - The evolution of the underground economy expressed as a percentage of GDP for the 28 EU Member States in 2017

Source: Author's own processing based on the data in Table 2

According to the graph above, in 2017, Romania was second in Europe in the underground economy. According to a report by the European Commission, only Bulgaria is better than us at evasion and black work.

Romania "beats" with Bulgaria for the first place in the top of the European Union states when producing the underground economy. Our country is in second place, with 26,3% of GDP.

On the other side, that is the states with the lowest values, are Austria and Luxembourg (as specified above). A publication in the National Journal specified in 2017 that this phenomenon will "swallow" about 18 billion euro.

III. AT THE NATIONAL LEVEL

III.1. TAX EVASION

In Romania, the economic agents are "scared" by the exaggerated size of some taxes and duties, which led to the registration, at an alert rate, of the "offshore" companies, through which they carry out the crime of money laundering and fiscal fraud, the Romanian state being harmed by important money resources.

Offshore companies "are international companies registered in a country other than the one of origin," (the reason for registering a company abroad and not in the country of origin, where it operates, is the payment of a tax rate on the lowest profit realized).

These companies are registered in countries with permissive legislation and with very low taxation, these countries are represented by the so-called "tax havens".

"The operating principle of an offshore company is simple: the profit realized after carrying out the activity in the country of origin is transferred to the tax haven where the company is registered, this being obliged to comply with the financial legislation of the <adoptive country>" (Ardelean, Roată, Ardelean, Chiș & Stoica, 2014: 65).

The types of offshore companies used are: "non-resident company, International Business Company (I.B.C), exempt companies, LLT (Limited Liability Company), trust" (Ardelean, Roată, et al, 2014: 66).

In the Figure 2 will present the evolution of the tax evasion in Romania during the period 2004-2013:

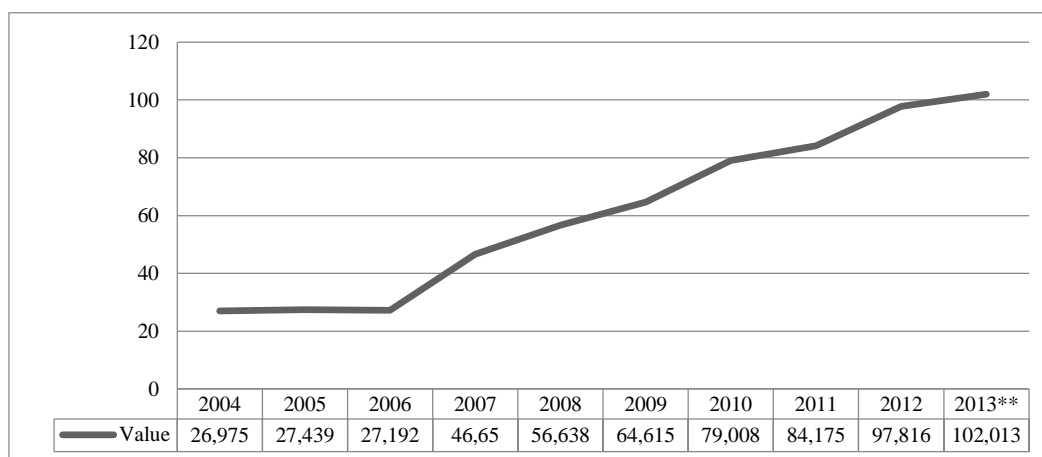


Figure 2 - The evolution of the tax evasion in Romania for the period 2004-2013

Source: Author's own processing after: Olteanu & Pascu, 2017: 280

*** we want to specify that we could not go with the analysis beyond 2013, because we did not have access to information - In the 2016 annual report, the Fiscal Council mentioned that: "The analysis regarding the financial performance of state-owned companies as well as the one regarding the estimation of the tax evasion in Romania will be finalized later, to the extent that the entry data will be available." "The reports for the years 2015 and 2016 no longer provide detailed information on the availability of the statistical data needed to issue the tax evasion."*

There is an unfavorable evolution of this phenomenon for Romania. The tax evasion being in a continuous increase in the analyzed years.

From year to year the phenomenon increases threateningly, from 2004 to 2013 the value of the phenomenon increases by 75,038 billion lei.

If, in the first year of the analysis, the evasion was 26,975 billion lei, in 2013 it presents a very high value of 102,013 billion lei.

We observe the increase of this phenomenon. It seems that during the first two years the tax evasion could have been under control, with no significant increase. Since 2006, the euphoria phenomenon has had an unfavorable evolution, growing significantly.

In the previous graph the total tax evasion was presented. We have chosen to show in the following table and graph (Table 3 and Figure 3) which are the main taxes and duties from which taxpayers are evaded.

Table 3. Tax evasion on the main taxes and duties

Millions LEI	The year									
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
Work in the black	4.278	4.546	5.891	7.671	8.973	14.652	16.665	17.510	16.966	16.414
Income tax	1.831	1.365	1.798	2.392	3.009	4.366	5.093	4.968	4.852	4.749
Contributions to social insurance	4.324	5.037	6.267	8.015	9.357	14.052	16.393	15.989	15.617	15.285
VAT	18.683	18.050	15.067	29.982	38.085	40.156	50.347	57.476	72.399	76.747
Profit tax	1.351	1.780	2.555	3.126	3.993	3.237	3.512	3.126	2.624	2.795
Excise duties and the tax on vice	786	1.207	1.505	3.137	2.194	2.805	3.663	2.616	2.323	2.438

Source: Author's own processing after: Dan, 2017: 23

The table above shows that the value added tax comprises most of the evasion, it is followed by the black work, the 3rd place is occupied by the social insurance contributions. The last position is occupied by excise duties and the tax on vice.

The main method related to fraud is the value added tax. This decreases in 2005 compared to 2004 with 633 million lei, and then increases from one year to another until reaching, in 2013, a value of 76.747 million lei.

The work in black, records fluctuating values increasing in the first 8 years analyzed and diminishing in the last two years. It is closely linked to social security contributions, being the main cause with an important role in increasing evasion.

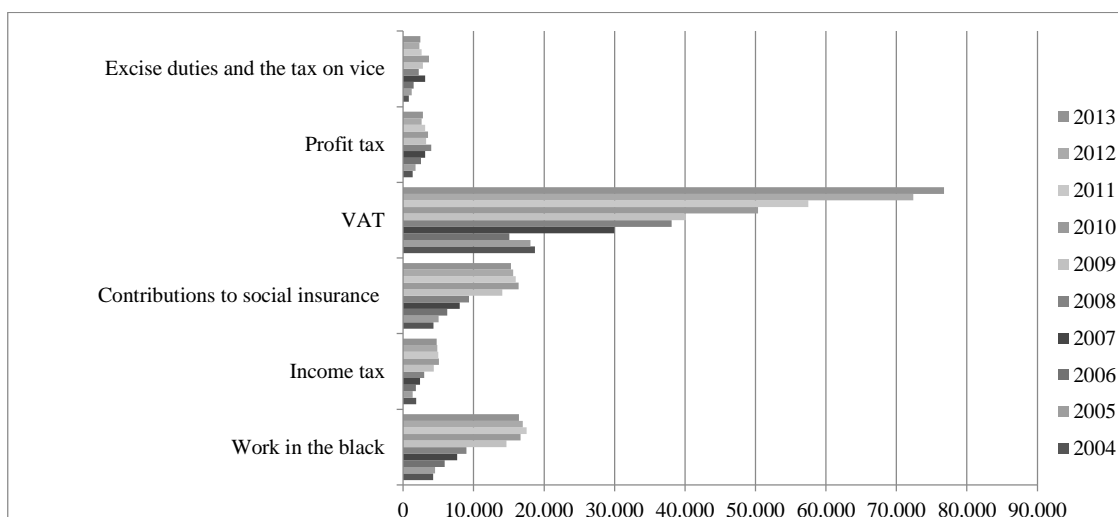


Figure 3 - The evolution of tax evasion on the main taxes and duties

Source: Author's own processing based on the data in Table 3

The ones mentioned in the interpretations of the above table (see Table 3) are avoided by making this graph.

VAT and black employment are on the rise. The other taxes and duties recorded oscillating values during the 10 years subjected to the analysis.

III.2. THE UNDERGROUND ECONOMY

The fiscal policy processes suggest that a moderate reduction in taxes, together with a stronger effort in the monitoring process, causes a considerable reduction in the size of the underground economy and provides a positive incentive for the ordinary economy (Orsi, Raggi & Turino, 2014: 417-436).

The underground economy is reflected in the discrepancies that appear in different markets. People who work in the unofficial sector can spend more than the officially registered income. The difference between the two can be observed in the individual households, as well as in the global national accounts. This approach is debatable, as this discrepancy between income and expenditure may be due to either measurement errors (most often) or reasons not related to the underground economy (for example, the use of credit or the reduction of wealth) (Frey & Schneider, 2015).

The level, dynamics and evolution of the underground economy at national level will be recorded in the Figure 4, as follows:

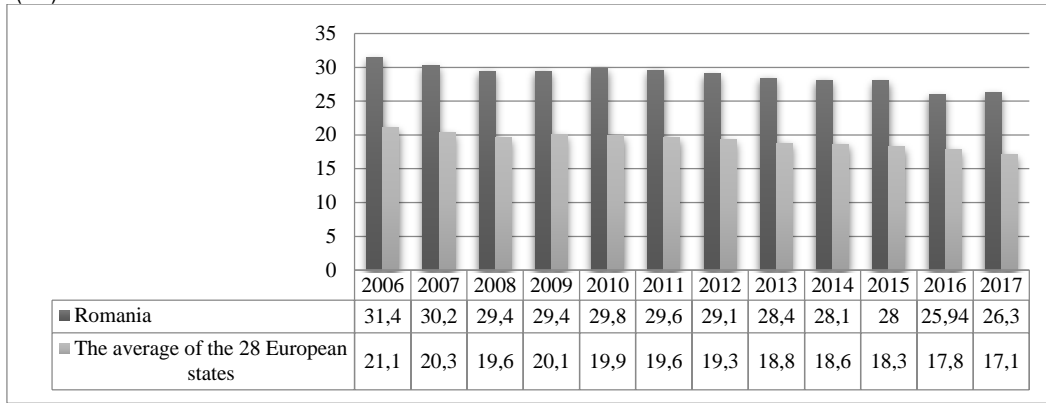


Figure 4 - The evolution of the underground economy expressed as a percentage of the GDP, from Romania compared to the EU average, between 2006-2017

Source: Author's own processing after: Grosu, 2018: 3

At the moment when the accession to the EU was taken into account, the economy was reduced by about 5,1%. This decrease is also due to the extension of electronic payment services.

Following the analysis of this chart we can say that, regarding the underground economy, the situation of Romania is worrying. The values registered for Romania exceed the average of the European Union in every year.

Every year of the analysis, Romania's underground economy is about 10% higher than the EU average.

The highest value, of 31,4%, is recorded in the first year of the analysis, and the smallest value in the last year, of 26,3%.

It can be noticed, a tendency of decrease, thus, from the percentage of 29,8% in 2010, it reaches 26,3% in 2017, having a decrease of 3,5%. Although the underground economy in Romania has a downward trend, it continues to be above the European average.

IV. CONCLUSIONS

Conducting the research has led to the achievement of the proposed objective, namely to determine and present the level and evolution of tax evasion and the underground economy at the level of all EU Member States.

We have studied the level of the underground economy at European and national level. This is manifested in all branches and in all sectors of the economy, and among the causes that determine it are: fiscal pressure, corruption, poverty level, unemployment rate and the desire to earn.

The Romanian state is one of the EU member states with big unresolved issues in managing tax evasion. It is a phenomenon that is growing in our society, helped by fiscal corruption, the bureaucracy of the public system and the resignation of the control bodies, through a reluctant attitude.

Tax evasion is a complex phenomenon, which undoubtedly has many negative effects and undesirable implications on the economy and society being present both economically and socially.

We consider that for fighting tax evasion is not necessary to impose drastic sanctions, but it should be realized, from our point of view, an efficient and effective fiscal control, it would be necessary to implement a viable legislative system and simple, clear, precise, and relatively stable tax laws and achieving a better tax education of citizens.

According to the Fiscal Council, the main solutions to diminish the unobserved economy could be:

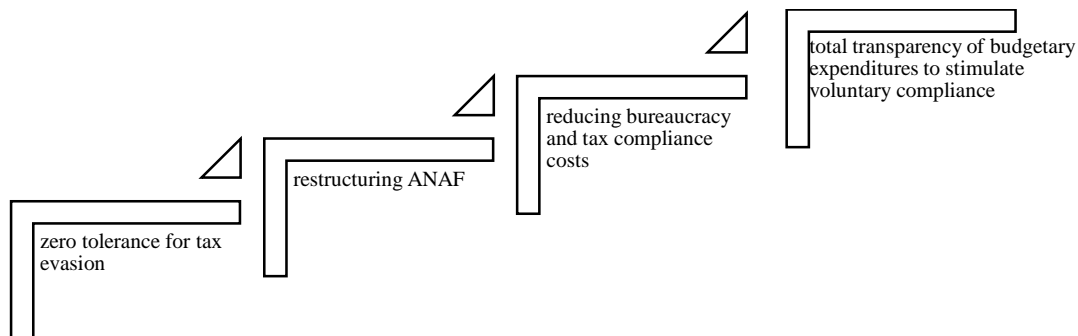


Figure 5 - Solutions for diminish the informal economy

Source: Author's own processing after: Dumitru, 2018: 35

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