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## Tax Evasion in Romania

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### Abstract

Tax evasion cannot be totally eliminated but it can be reduced due to better legislation and better fiscal politics. It is necessary to unify the fiscal and financial legislation with the elaboration and adoption of a new Fiscal Code where the bonds, the procedure for their determination and imposition, the taxpayers' rights and obligations as well as the fiscal organisms' rights and obligations, crimes and other sanctions according to constitution provisions must be regulated.

**Keywords:** Tax Evasion, Fraud, GDP, Law, Taxpayer

### Introduction

Tax evasion is of two types: legal tax evasion and illegal tax evasion.

Legal tax evasion is possible when law is incomplete or evasive and takes place when part of the income or wealth belonging to certain people or social strata is a source for taxation.

Illegal tax evasion means to willingly hide the taxation object by under evaluating the sum of the taxable matter or using other means to circumvent the payment of taxes, fees and other duties<sup>1</sup>.

In specialised literature, there are a number of fiscal fraud types:

- *Long term fraud* – economic agent which has obtained good reputation along time due to its behaviour and results. It abruptly stops payment, is declared in case of bankruptcy after the profit has previously transferred in another country.

- *Short term fraud* – a new founded enterprise issues the fiscal organisms a justified requirement for VAT refund but after the refund, the company ceases to function and the payer disappears.

- The "*Phoenix*" Syndrome – a firm which is bound to play the VAT declares bankruptcy but another company led by the same manager is founded.

- The "*multiple companies*" syndrome – among several registered firms, one is a dummy corporation

- *Insignificant manipulation* –repeated registration of invoices, wrong reports, and payment documents factiously dated<sup>2</sup>.

<sup>1</sup> Bistriceanu Gh. (2009). The fiscal system in Romania, pp. 340-342.

<sup>2</sup> Mosteanu N.R. (2008). Fiscality -Taxes and Fees, Universitara Printing House, pp. 85-86.

In general it is difficult to determine all means of evasion of this type as they are limitless. Within fiscal activity, there are more frequent means of evasion:

- issue of false statements;
- issue of fictitious payment documents;
- issue of fictitious bookkeeping;
- non declaration of taxable matter;
- declaration of less income than the real income;
- issue of double bookkeeping, real and fictitious registers;
- diminution of imposable matter due to less turnover by registering fictitious expenses;
- sales without invoice, as well as issue of invoices for fictitious sales which hide real operations due to taxation;
- false balance sheet as means of fraud for the IRS, which is an agreement between the manager and the senior accountant, thus making the accountant sole responsible for the deed<sup>3</sup>.

### **Effects of Tax Evasion**

Tax evasion is growing and is gaining more and more power in fighting the state institutions. Why isn't anybody willing to stop it? Because due to tax evasion, a lot of the law administrators have bought houses, expensive cars and spend holidays abroad. Why is the controlling bodies' income not verified? It is not verified because nobody desires to do so as these claws of tax evasion have hooked most of them. The money due to the state budget is gathered by them.

The issue of tax evasion has been politically supported, tolerated, avoided and postponed for 23 years. At present, in full financial and economic crisis, there must be taken firm action in a least two major directions of hidden economy: underground labour and tax evasion with the purpose of obtaining a public budget oriented towards competition, cooperation, investments, economic growth, transparency and honesty.

In general, in acute crisis situations, here including the present case of Romania, space is compressed to the citizen's hard-fisted purchase power. As a result, firm actions must be taken. On the one hand, they should encourage the business environment in order to avoid the growth of budget rise by means of new taxes and fees, some of them illogical and on the other hand, the payment of pensions, salaries and shares for major investments in infrastructure, culture, cults, education, research and health.

In this sense, the budget expenses which have to be done in reasonable limits must be income deriving also from the present fiscal system. In the present moment, regarding the fiscal burden, the number one priority of the Government is to reduce to a minimum the activity of the underground economy! In other words, the underground economy must resurface in order to see how deep the underground economy fraud is.

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<sup>3</sup> Bistriceanu Gh. (2009). The fiscal system in Romania, pp. 340-343.

Table 1. Evolution of IPC for the EU states between 2008-2010

	2008	2009	Modification 09/08	2010	Modification 10/09
Denmark	9,3	9,3	0	9,3	0
Sweden	9,3	9,2	-0,1	9,2	0
Finland	9	8,9	-0,1	9,2	0,3
Holland	8,9	8,9	0	8,8	-0,1
Luxembourg	8,3	8,2	-0,1	8,5	0,3
Germany	7,9	8	0,1	7,9	-0,1
Ireland	7,7	8	0,3	8	0
Austria	8,1	7,9	-0,2	7,9	0
U.K.	7,7	7,7	0	7,6	-0,1
Belgium	7,3	7,1	-0,2	7,1	0
France	6,9	6,9	0	6,8	-0,1
Slovenia	6,7	6,6	-0,1	6,5	-0,1
Estonia	6,6	6,6	0	6,5	-0,1
Cyprus	6,4	6,6	0,2	6,3	-0,3
EU 27	6,51	6,36	-0,15	6,3	-0,06
Spain	6,5	6,1	-0,4	6,1	0
Portugal	6,1	5,8	-0,3	6	0,2
Malta	5,8	5,2	-0,6	5,6	0,4
Hungary	5,1	5,1	0	4,7	-0,4
Poland	4,6	5	0,4	5,3	0,3
Czech	5,2	4,9	-0,3	4,6	-0,3
Lithuania	4,6	4,9	0,3	5	0,1
Slovakia	5,9	4,5	-1,4	4,3	-0,2
Latvia	5	4,5	-0,5	4,3	-0,2
Italy	4,8	4,3	-0,5	3,9	-0,4
Greece	4,7	3,8	-0,9	3,5	-0,3
Romania	3,8	3,8	0	3,7	-0,1
Bulgaria	3,6	3,8	0,2	3,6	-0,2

Data source: *Transparency International Romania*

Table 2. Dimensions of underground economy in 2009

Country	GDP
Great Britain	15-20%
Italy	30%
Germany	20%
USA	26%
Spain	19,2%
Bulgaria	32,6%
<b>Romania</b>	<b>30%</b>
Switzerland	8,1%

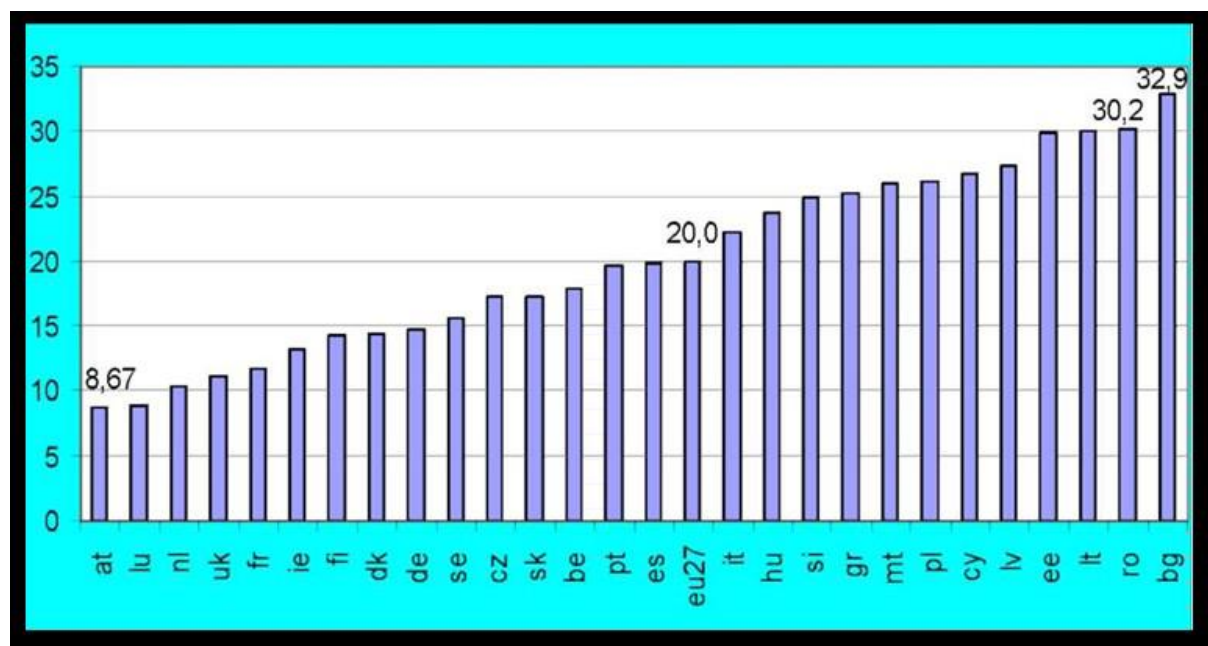


Figure 1. Underground economy in the EU member states in 2010

*According to the estimates issued by PhD Prof. Friedrich Schneider, University of Linz/AUSTRIA*

From a macroeconomic point of view, the estimates of fiscal fraud (especially from VAT) represent 5%-6% of GDP and underground economy to about 23% of GDP in the last years.

In the view of the controlling body, safest evaluation of fiscal evasion level is given by real results based on the number of criminal complaints, the value of the prejudice and the value of the sequestered merchandise or contraband, etc.

From the budget point of view, we can simply compare to our neighbouring country, Bulgaria, which has a sole percentage of 10% and 20% VAT and a budget income of about 40% of the GDP while in Romania, budget tax collection represents only 32%, when the sole quota is represents 16% and VAT represents 24%. We are definitely not taking into account the differences of the other taxes but they are giving us an entire view over the phenomena.

In the field of intra communitarian merchandise acquisition, by skipping the VAT payment in the trade with energetic products, alcohol and tobacco, generally the highest taxed merchandise is in the agricultural trade and not only.

The rising tendency has almost entirely stopped by the undertaken actions in the field of cereal, food and communitarian products trade as well as from the tobacco trade which make up the most exposed fields to underground trade. The macroeconomic estimates of these evasion activities will be known by the end of this year.

The control and inspecting activities highly hardened in 2009 and mainly regarded the taxpayers highly oriented towards tax evasion and fraud, selected based on risk analysis.

The service of monitoring fiscal activities which acts within the Fiscal Information Department, which is part of ANAF (National Agency for Fiscal Administration - NAFA) since 2007 has as main duties international exchange of fiscal information, intra communitarian cooperation fir VAT and risk analysis. The activities of the new service is done exclusively and mainly means to: identify data sources for foreign fiscal information beyond NAFA necessary for the good functioning of the agency; analysis, verification, evaluation, and coordination of

the data obtained with the fiscal information detained by NAFA; management of information exchange protocols of NAFA with the other institutions of the Ministry of Labour, HDM etc. All these activities have a sole purpose: to grow of efficiency and fight tax evasion.

Let us see a few examples which show that it all about bad faith and corruption and not inability on the authorities' behalf. Colentina is the paradise of the invoice and receipts sellers for tax evasion practitioners. They operate right under the police nose. Why are they left alone? Are they left alone because they pay a tax to the police? It seems so because otherwise I do not believe that all the police is incompetent.

Prostitution is another field where nice money is made. The „girls” are always fined but the “pimps” are never caught. Why is that?

We see that more and more corrupt policemen and prosecutors on TV. Only those who keep everything for themselves are caught as they do not pay the others. But life goes on and so does tax evasion.

Another field where tax evasion is at home is the production and commerce of alcohol. After the revolution, those who bottle vodka, rum or any other booze used to do it in bathtubs and wash basins. Now they have real small plants hidden in different yards at the city outskirts. Here tax evasion represents 40 %, which equals over one percent of the GDP.

“Tax evasion on the bread manufacture field is about 70%. The lack of budget payment in this field is of 1 billion Euros per year and another billion Euros is missing from the budget in the field of agriculture for the same reason – tax evasion”(said president of ROMPAN, Aurel Popescu, with the occasion of the debate "Crisis solutions").

The commerce of merchandise in Europa commercial centre is mainly done without invoices. How have they managed so far? The people who sell there say that they pay the controlling bodies every week and month. But if not caught red-handed, you're a fair trader, aren't you? In our case, the uncaught thief is a tax evasion practitioner.

Who practices tax evasion in nowadays Romania? The greengrocer from the market, the retailer, the street commerciant, the plumber, the corner shop seller, the waiter who serves you in the restaurant or bar and gets tips, the employer who pays higher salary than stipulated in the contract, the farmer who sells his goods without declaring his income, the owner of the apartment where you pay the rent, the old lady who sells milk, cheese and cream every Thursday, and so on. All these people are tax evasion practitioners<sup>4</sup>.

The taxes and fees are a heavy burden for the Romanian employers. The economic crisis has heightened the number of the Romanians working underground. The Romanian state records loss of 18 billion Euros/year from tax evasion. The number of the Romanians who work underground exceeds 2.3 million, which is more than a third (35.3%) of the total of employees by comparison to 900,000 in 2008, according to the report issued by the Fiscal Council.

## Conclusions

The report at the end of 2011 sows that:

- 6.647 million people were employed and the employers reported a number of 4.297 employees. Thus, 2.348 million people were working underground;
- tax evasion from underground work equalled 30,842 billion leis in 2010;
- tax evasion to VAT equalled 18,766 billion lei;

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<sup>4</sup> Stefan Murgeanu, Financial education, 12.01.2012



- tax evasion in the informal sector (population) – 4.076 billion lei<sup>5</sup>.

In conclusion the state employees' salary cuts, pension cuts, unemployment aid and subventions brought about 2.5% of GDP to the state budget but have brought serious social issues. Was it not easier that this GDP percent be obtained by cutting tax evasion?

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<sup>5</sup> Report of the Fiscal Caouncil