



## ORIGINAL PAPER

# Fiscal policy and tax evasion in the context of COVID-19 pandemic

**Cristi Spulbar<sup>1)</sup>, Ramona Birau<sup>2)</sup>, Petre Valeriu Ninulescu<sup>3)</sup>**

### **Abstract:**

The aim of this research study is to provide a comprehensive theoretical analysis on the phenomenon of tax evasion, but also fiscal policy measures in the context of COVID-19 pandemic. Fiscal policy highlights the path of government authorities on economic activity based on public revenues and expenditures. The phenomenon of tax evasion significantly affects the prospect of sustainable economic growth. In order to ensure economic stability, it is very important for government authorities to apply rigorous measures to prevent and combat tax evasion.

**Keywords:** *tax evasion; extreme event; fiscal policy; COVID-19 pandemic; underground economy; government authorities.*

**JEL Classifications:** E62, F43

---

<sup>1)</sup> University of Craiova, Faculty of Economics and Business Administration, Craiova, Romania, Email: cristi\_spulbar@yahoo.com. ORCID ID 0000-0002-3909-9496.

<sup>2)</sup> University of Craiova, Doctoral School of Economic Sciences, Romania, C-tin Brancusi University of Targu Jiu, Faculty of Education Science, Law and Public Administration, Romania, Email: ramona.f.birau@gmail.com. ORCID ID 0000-0003-1638-4291.

<sup>3)</sup> Faculty of Economics and Business Administration, University of Craiova, Romania, Email: petre.pregi@yahoo.it.

## **Fiscal policy and tax evasion in the context of COVID-19 pandemic**

### **1. Introduction**

Economic growth exerts a major influence on evolution of real income. In other words, the relationship between the two variables is essential, namely: fiscal policies and economic growth. Budget revenues and expenditures have certain characteristics that are influenced by the economic cycle. Tax evasion is a topic of great current interest. Fair taxation is a priority for most countries in the world. Public spending and tax revenue are levers used by government authorities to influence economic growth. The evolution of budgetary revenues and expenditures is influenced both by the dynamics of the volume of economic activity and by the decisions of the governmental authorities.

On the other hand, contractionary fiscal policy serves the measures implemented by government authorities in order to temper (slow down) the economic growth. These strategies of government authorities are based on decreasing public spending or increasing tax revenue, but a mix of these previous directions is also possible. Fiscal policy represents a mix of government measures focused on taxes, given the role it plays in shaping budget revenues and financing budget expenditures. Fiscal policy is the prerogative of the government and is a form of indirect state intervention in the economy, and through it, a government ensures the maintenance of macroeconomic balance. For example, the decision to increase or decrease the level of investment is influenced by the effective marginal tax rate. In other words, the lower is the effective marginal tax rate, the more favorable the tax regime is for investments, and vice versa.

Extreme events massively influence a country's economic and financial measures, as was the case with the recent global financial crisis (GFC) of 2007 - 2008, but also with the COVID - 19 pandemic. The economic crisis caused by the COVID - 19 pandemic has significantly affected most countries in the world. The COVID 19 pandemic is a global source of stress for both the population and governments, including health systems, business, tourism, financial system, industries and others.

### **2. Literature review**

Zasko et al. (2021) have conducted an empirical study for Russia but also globally, considering tax system digitization, budget efficiency and customs administration. Digital economy and digital information exchange system represent key aspects for improving to improve the level of revenue and tax collection from taxpayers. Moreover, Isaev et al. (2021) also investigated certain aspects regarding the expenditure of public resources in the case of Russia and emphasized the importance of ensuring the “expediency, legality, and efficiency of the generation, distribution, and use of budget resources”.

Kim and Im (2017) examined the impact of Corporate Social Responsibility (CSR) on tax avoidance contributor (tax payer) behaviour and concluded that common equity growth has developed a negative connection with corporate tax avoidance by also considering the concept of financial ratios in this regards. Ji and Zhang (2020) have conducted an empirical case study for China and concluded that value - added taxation exhibits an important influence on the “gap between land urbanization and population urbanization”.

Hasanov et al. (2018) examined the impact of fiscal policy in the case of a developing country such as Azerbaijan and argued that government authorities have the opportunity to lead available public resources for adjustment of the economy based on certain measures like monetary and fiscal policies. Caballero (2013) investigated

relevant aspects regarding the implications of fiscal policy during the period of Great Recession and suggested that “fiscal policy is an appropriate countercyclical policy tool under some circumstances”. Tosun and Yildiz (2020) argued that tax policy uncertainty has the ability to influence certain business companies (firms) to take lower risks and as a consequence to decrease the possibility of debit and implicitly the degree of default.

Zhou et al. (2019) investigated the impact of fiscal policies on environmental pollution control in the case on China considering the importance of the intervention of the governmental authorities through active measures in environmental protection. Jiang et al. (2019) also discussed important aspects regarding Chinese fiscal decentralization in the context of environmental pollution as well as the implementation of regulatory reforms in this regards. Ziolo et al. (2020) investigated the linkage between certain key factors such as public financial system, financial development, fiscal levers, public income and expenditure, and environmental degradation and pollution, taxation system in the case of European Union member states for the sample period from 2008 to 2017.

Hsing (2013) analyzed the impact of fiscal policies on the dynamics of the stock market from Poland and concluded that the fiscal policy based on ratio of government deficit or considering the debt to Gross Domestic Product (also known by the acronym GDP) does not exert a major effect on the behaviour of the selected Polish stock market index. Ji and Zhang (2020) argued that certain government authorities whose strategies are characterized by a lower fiscal self - financing rate are affected by a higher fiscal pressure so it is necessary to identify additional public revenues.

Spulbar et al. (2021) conducted a complex research study on the European Union but also discussed the role of taxation which addresses the following essential aspects, i.e.: to provide the public revenues for government spending, to determine redistribution of public incomes, to generate economic stability, to streamline the allocation of public resources and to contribute to economic growth.

### **3. A conceptual analysis on fiscal policies and tax evasion**

As a practical approach, the concept of tax avoidance represents the linkage between two other very representative terms in the understanding of tax evasion, such as tax evasion and tax saving. Tax avoidance obviously involves eluding the legal regulations in the fiscal field. Kim and Im (2017) defined the concept of tax avoidance as the special situation in which a company / firm “can either explicitly or implicitly reduce its tax burden without incurring additional expenses from tax investigations, in both the short-term and long-term”. Practically, taxation encompasses all taxes imposed on the citizens of a state. Thus, tax evasion is a deviation from taxation that involves operating in a normal system of taxes.

Taxation is an essential factor in ensuring a fair and non-discriminatory society. For example, excessive, legally flawed and unpredictable taxation can lead to macroeconomic imbalances. Taxation must ensure the establishment of equal treatment for all taxpayers. Another very important aspect that government authorities must take into account is the establishment of a level of taxation based on objective and equidistant financial criteria in order to ensure a macroeconomic balance. Also, the fiscal policy must be proportionate, predictable, reasonable, fair and not differentiate taxes on the basis of categories of taxpayers according to certain factors.

On the other hand, the lack of stability and predictability are aspects that generate imbalances caused by fiscal policies on macroeconomic framework and implicitly affect the prospects for sustainable economic growth. Fiscal policy can have a

## **Fiscal policy and tax evasion in the context of COVID-19 pandemic**

major influence on employment decision-making, reducing unemployment, and improving investment levels. As an effective lever, fiscal relaxation is necessary and applied by government authorities to stimulate the economic growth.

According to the official website of European Commission, national governments have the major task of collecting taxes and setting tax rates by considering the fact that European Union (EU) has no direct role in this regards. Moreover, the European Union play a role in coordinating certain national taxation rules, but also some tax rates, where differences may discourage citizens to carry out a particular commercial activity based on buying and / or selling in other EU countries. The European Union also promotes cooperation between member states on combating tax fraud and tax evasion, by eliminating discrimination and reducing the costs of compliance tasks. On the other hand, the EU provides Member States with a legislative framework that allows them to combat cross-border tax fraud and tax evasion in a coordinated manner.

The phenomenon of tax evasion has severe implications for sustainable development and economic growth. Tax evasion represents the attempt of a tax payer (individual or legal entity - company, firm and so on) to evade the payment of its fiscal obligations by not declaring certain parts of income or profits that need to be stipulated for the proper functioning of the tax system. The indisputable negative effects generated by the phenomenon of tax evasion are directly manifested on the level of tax revenue receipts, causing significant distortions in the mechanism of market functioning. Gorun et al. (2020) also argued that tax evasion significantly affects the activity of raising budget revenues, aspect that generates economic instability.

In addition, the extended form of tax evasion includes, in particular, the category of missing trader fraud. In the case of European Union, the concept used is missing trader intra - community fraud. The reduced form of evasion, is the one developed by the retail trader who sells products and services without issuing the tax receipt. The solution in terms of combating the reduced form of tax evasion involve binding the issuance of the tax receipt prior to the collection of the product price and the application of severe sanctions for non-compliance (starting from high fines to criminal penalties based on imprisonment).

Measuring tax evasion is done through the underground economy that is, those illegal economic activities. In financial literature and practice similar concepts with underground economy are also used, such as: informal economy, grey economy, black market or shadow economy. When the average tax burden is relatively high, then the taxpayer can choose to evade this taxation, either in full dimension as to entry into the underground economy or in part, by practicing legal tax evasion even if his activity remains in the white economy, such as in the case of tax heavens. Meher et al. (2021) conducted an empirical study on digital banking and its impact on micro, small and medium enterprises (MSMES) because it provides a series of facilities to customers but also has an essential role in reducing tax evasion by avoiding the use of cash payments.

### **4. Conclusions**

The economic growth is significantly influenced by the effectiveness of the implementation of fiscal policy measures. The quality of taxpayer services is a significant factor contributing to the improvement of taxpayers' voluntary compliance. The economic programs of government authorities are identified in fiscal policies. Thus, fiscal policy allows legal regulators to influence the business cycle, unemployment rates, interest rates, and inflation in an attempt to maintain a macroeconomic balance.

Tax evasion is one of the most toxic economic and social phenomena, especially important in the context of taxation, which affects countries all around the world. However, government authorities need to take very firm and effective action in order to combat tax evasion. Accurately measuring the level of tax evasion and the underground economy is a difficult and challenging task especially in the context of an extreme event such as the COVID pandemic - 19.

#### Authors' Contributions:

The authors contributed equally to this work.

#### References:

- Caballero, G. (2013). "Effects of Fiscal and Monetary Policy in the Great Recession", *Economies*, 1, 15 – 18, EISSN 2227-7099, published by MDPI, <https://doi.org/10.3390/economies1020015>.
- Gorun, T.H., Spulbar, C., & Birau, R. (2020). "General conditions for engaging the criminal liability of the legal persons based on penal laws and fiscal legislation: A case study for Romania", *Revista de Științe Politice. Revue des Sciences Politiques*, 67, 92 - 102.
- Hasanov, F., Mammadov, F., & Al-Musehel, N. (2018) "The Effects of Fiscal Policy on Non-Oil Economic Growth", *Economies*, published by MDPI, 6, 27, <https://doi.org/10.3390/economies6020027>.
- Hsing, Y. (2013) Effects of Fiscal Policy and Monetary Policy on the Stock Market in Poland, *Economies*, published by MDPI, 1, 19 -25, <https://doi.org/10.3390/economies1030019>.
- Kim, J., & Im, C. (2017) "Study on Corporate Social Responsibility (CSR): Focus on Tax Avoidance and Financial Ratio Analysis", *Sustainability*, 9, 1710. <https://doi.org/10.3390/su9101710>.
- Isaev, E.A., Fedchenko, E.A., Gusarova, L.V., Polyakova, O.A., & Vasyunina, M.L. (2021) "Performance audit in the public sector: Domestic and foreign experience Auditoría de gestión en el sector público: Experiencia nacional y extranjera", *Studies of Applied Economics*, 39, 24, ISSN: 1133 – 3197, ISSN: 1697 – 5731.
- Ji, L., & Zhang, W. (2020) "Fiscal Incentives and Sustainable Urbanization: Evidence from China", *Sustainability*, 12 (1), 103, <https://doi.org/10.3390/su12010103>.
- Jiang, K., You, D., Merrill, R., & Li, Z. (2019). "Implementation of a multi-agent environmental regulation strategy under Chinese fiscal decentralization: An evolutionary game theoretical approach", *Journal of Cleaner Production*, 214, 902 – 915, <https://doi.org/10.1016/j.jclepro.2018.12.252>.
- Meher, B.K., Thonse, H.I., Latasha, M., Spulbar, C.M., Birau, F.R., & Rebegea, C. (2021) "The Impact of Digital Banking on the Growth of Micro, Small and Medium Enterprises (MSMES) in India: A Case Study", *Business: Theory and Practice*, 22 (1), 18 – 28, Doi.org/10.3846/btp.2021.12856, Available at SSRN: <https://ssrn.com/abstract=3770889>.
- Spulbar, C., Ehsanifar, M., Birau, R., Babaie, A., & Doagă, D. I. (2021). "Advanced empirical research based on structural equation modeling (SEM) regarding the impact of tax revenue on GDP dynamics at EU-28 level", *Scientific Annals of Economics and Business*, 68(3), 285 - 307, <https://doi.org/10.47743/saeb-2021-0017>.

## Fiscal policy and tax evasion in the context of COVID-19 pandemic

- Tosun, M.S., & Yildiz, S. (2020). "How Does Aggregate Tax Policy Uncertainty Affect Default Risk?" *Journal of Risk and Financial Management*, 13 (12), 319, <https://doi.org/10.3390/jrfm13120319>.
- Zasko, V., Sidorova, E., Komarova, V., Boboshko, D., & Dontsova, O. (2021). "Digitization of the Customs Revenue Administration as a Factor of the Enhancement of the Budget Efficiency of the Russian Federation", *Sustainability*, 13, 10757, <https://doi.org/10.3390/su131910757>.
- Zhou, C., Xie, H., & Zhang, X. (2019). "Does Fiscal Policy Promote Third-Party Environmental Pollution Control in China? An Evolutionary Game Theoretical Approach", *Sustainability*, 11, 4434, <https://doi.org/10.3390/su11164434>.
- Zioło, M., Kluza, K., Kozuba, J., Kelemen, M., Niedzielski, P., & Zinczak, P. (2020) "Patterns of Interdependence between Financial Development, Fiscal Instruments, and Environmental Degradation in Developed and Converging EU Countries", *International Journal of Environmental Research and Public Health*, 17 (12), 4425, <https://doi.org/10.3390/ijerph17124425>.
- \*\*\* - [https://ec.europa.eu/info/policies/taxation\\_ro](https://ec.europa.eu/info/policies/taxation_ro) - official website of European Commission - European Union (EU)

---

### Article Info

*Received:* February 27 2022

*Accepted:* March 08 2022

---

#### **How to cite this article:**

Spulbar, C., Birau, R., Ninulescu, P. V. (2022). Fiscal policy and tax evasion in the context of COVID-19 pandemic. *Revista de Științe Politice. Revue des Sciences Politiques*, no. 73/2022, 32-37.