Research Article

Income concealment and its impact on the Economy

Skerdian Kurti
Faculty of Law, University of Tirana

Arnold Visha
Lalaj CPA Group

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Abstract

The revenues collected from taxes and levies constitute the largest part of the State budget. These revenues are significant as, without them, the State's financial activities cannot be carried out, nor can the public needs of society be met. More revenue from taxes and levies means more schools, kindergartens, nurseries, hospitals, roads, and more services for the community, drafting effective social and criminal policies to protect individuals and society. For this purpose, it is important not only to determine the level of taxes and levies but also to protect their collection to ensure the necessary services for the benefit of society. One way to protect tax and levy collection is through criminal legislation. Among the criminal offenses provided for this purpose, Article 180 titled "Income Concealment", which punishes all illegal behaviors that favor tax evasion, is of great importance. Through this paper, we aim to present the direct importance of revenue collection for the economic and social development of a country by initially identifying some of the ways in which the criminal act of income concealment is committed by commercial companies. This paper will also include a brief analysis of criminal legislation protecting tax revenues before moving on to the economic analysis of tax evasion and the difficulties encountered in combating this phenomenon.

Keywords: Taxes, levies, economy, economic crime, criminal law.

1. Introduction

Income concealment or "tax evasion" as it is otherwise known, falls under the category of criminal offenses that are part of a broader category of crime known as "economic crime". This type of crime includes all forms of criminal activities oriented towards the national economic system and its functioning. Key characteristics of this crime are "dark figures", dynamics, and adaptation to all economic and regulatory changes (Alessandri, Seminara, 2018).

According to Albanian legislation, a levy implies a compulsory levy in favor of the State budget, which the public entity may impose on certain subjects in an institutional manner, and which is designated by law for the realization of an income. It refers to compulsory and non-refundable payment, without needing the consent of the private party. However, the justification for this category of income and consequently the understanding of the tax seems to be continually subject to various modifications depending on political considerations regarding the reasons for the fiscal sacrifice. A tax, meanwhile, is understood as the payment made in exchange for which the person benefits from a service from the institution in favor of which the tax is paid (Gjyli, 2009).

Income concealment can be complete or partial, but both cases are against the law and punishable. We deal with complete evasion when: the taxpayer does not declare the entire amount of income realized that is subject to tax; he does not fully declare the property he owns; he conceals events or facts that have to do with the tax. On the other hand, evasion can be partial when: the taxpayer declares only part of the amount of income realized that is subject to tax; he declares his property only partially; he partially conceals events or facts that have to do with the tax.

Through the revenues realized from the collection of taxes and levies, significant interventions can be made in key sectors of the economy and towards improving the standard of living in society. With the help of taxes, the State influences the volume and structure of investments, steering them towards branches and sectors where society has the greatest interest and benefit. Through taxes, the mitigation of inflation is aimed at, and the avoidance of factors that cause disruption of balances and difficulties in the economy. Alongside their undeniable role in the economy, taxes and levies remain also significant instruments for the realization of the State's social policies. Through the collection of taxes and levies, the State provides services and goods to the public. There are certain types of services and goods that by their nature can only be provided by the State such as national defense, public safety, judicial services, and services offered by the state administration. These revenues benefit the entire society and not just an individual. Therefore, to finance their cost, the State uses taxes and levies. Through taxes, social and economic welfare is ensured. Vital sectors such as education, health care, energy, and the environment are under the administration and care of the State. To effectively maintain these, the State is helped by the revenues collected from taxes. Through taxes, the redistribution of income is made possible. Social security depends directly on the system of taxes and levies. Therefore, the more taxes and levies are paid, the more secure this system will function, and the more secure our future will be. On the other hand, with the revenues obtained from taxes and levies, the State assists and supports low-income families or needy layers of society. The system of taxes and levies significantly influences the reduction of consumption or the complete avoidance of the use of some goods that adversely affect human health such as tobacco or alcohol (Kurti, 2018).

According to statistical data, globally, the value of tax evasion is equivalent to 427 billion dollars or 360 billion euros every year. The main evaders are commercial companies that transfer their profits to tax havens, not declaring them to competent national authorities and causing a budget revenue loss of 206 billion euros every year. Individuals who commit tax evasion are not far behind, amounting to 154 billion euros every year (Arcieri, 2020).

Some of the most used forms of income concealment encountered in practice include (Rakipi, 2003): non-declaration of personal income by individuals who are tax subjects or by their employers, (primarily commercial companies). This form of tax evasion is often linked to what is called "off the books" which brings negative consequences not only for the tax system but also for social security. Another form is non-declaration of income from customs, which, although it might initially seem like smuggling, often indirectly constitutes a case of income concealment because goods that enter circulation are not declared at customs, thus escaping declaration before the tax authorities. Non-declaration of subcontractors is most often encountered in entities engaged in major constructions, where large companies establish contractual relationships with smaller entities for various works. These smaller entities are not registered as taxable and operate under-the-table, allowing the larger entity to avoid tax obligations on these subcontracted works. Reporting losses in economic activity is a form of tax evasion widely used by commercial entities in our country through two main mechanisms: fictitious increase of expenses and non-invoicing of all sales made by the entity. The most common method to avoid VAT is the declaration of sales below their real value, using fake invoices not approved by the tax administration, meaning invoices with no tax value. Cash sales, not conducted through banks, allow sellers as well as buyers to avoid registering their entire activity in the accounting books, resulting in fewer or no incomes subject to taxes being declared, which complicates the control of financial transactions by the tax authorities.

2. Criminal defense against income Concealment

According to the prevailing opinion in society, income concealment benefits those who commit it but does not harm any other person. For this reason, the protective measures of individuals against this phenomenon are almost non-existent. Nonetheless, the illegal behavior of fiscal evaders increases the tax pressure on honest taxpayers. From this perspective, tax evasion would be ranked among those criminal acts that have a distributive effect (criminal acts with a distributive effect are those that remove material goods from some to give to others, such as theft, robbery, fraud) since it could harm all taxpayers proportionately (Kurti, 2018).

Income concealment is one of the most widespread crimes, and its presence has been noted since the creation of the tax and levy system. The significant importance of revenues obtained from the collection of taxes and levies is reflected in securing criminal protection by criminalizing those illegal behaviors that favor tax evasion to the detriment of creating the necessary revenues for achieving the important goals. According to data from the General Prosecutor's Office, during 2023, there were 187 criminal proceedings related to tax and levy crimes (articles 180-182/a of the Criminal Code), with 55 defendants. Tax and levy-related criminal offenses are found in Section IV of Chapter III of the Albanian Criminal Code, specifically articles from 180 to 182/a. According to doctrine, by criminal offenses related to taxes and levies, we mean those illegal acts (actions or inactions), committed intentionally and with the purpose of evading the payment of taxes and levies in various forms and manners (Elezi, 2008).

According to Article 180 of the Criminal Code ("Income Concealment"), *the concealment or avoidance of tax obligations through non-submission of necessary documents or non-declaration of necessary data, according to current legislation, submission of falsified documents, or false declarations or information, with the intent of material gain, for oneself or others, through the inaccurate calculation of the amount of tax, levy, or contribution, constitutes a criminal offense and is punishable by imprisonment up to three years. If this act is committed with the intent to conceal or avoid payment of a tax obligation of more than five million leks, it is punishable by imprisonment from two to five years. If this act is committed with the intent to conceal or avoid payment of a tax obligation of more than eight million leks, it is punishable by imprisonment from four to eight years*. To better understand the content of this provision, it is important to first analyze the terms used by the legislator "tax avoidance" and "tax evasion". Based on the practice of different states, we would find this definition for avoidance: "Tax avoidance" is the avoidance of the taxpayer from paying taxes without violating or conflicting with legal provisions. It appears in several forms: when the taxpayer changes the center of residence or business activity because in many cases the same activities carried out in different cities or regions also have different tax payments. Therefore, in this case, the law is not violated, but it is unfairly benefited from; when the taxpayer, by taking advantage of citizenship, creates a foreign company or foundation, which is not taxed in a specific country; when consumption is reduced or not all goods produced or imported are sold. The reduction of consumption for various reasons or not buying the entire quantity of goods automatically reduces the tax. In some cases, avoidance also occurs when one product is replaced with another; when deficiencies are found in the tax legislation itself: the taxpayer benefits from these gaps that the law itself creates for him and, with the help of legal advisors, avoids paying taxes; when the taxpayer, by exploiting legal gaps, makes technological changes in economic activity by producing goods that have a low tax. Thus, *tax avoidance* can be considered as an abnormal behavior towards social obligations, or in other words, as the right of every citizen to regulate his business in such a way that is allowed by law, but by paying fewer taxes and levies than required. Whereas by "tax evasion" we understand the efforts of every physical or legal person, who, to avoid paying taxes and levies, uses various ways contrary to the law. Tax evasion requires that taxpayers intentionally declare inaccurately or conceal the true state of their income before tax authorities with the aim of reducing the income that is subject to tax payment.

From an objective point of view, avoidance or evasion is carried out through non-submission of necessary documents or non-declaration of necessary data, according to current legislation, submission of falsified documents, or false declarations or information. In the case of commercial companies, this criminal offense may also compete with a series of other criminal offenses including, the creation of fraudulent schemes related to value-added tax (Article 144/a of the Criminal Code), abuse of power (Article 164 of the Criminal Code), providing false information (Article 168 of the Criminal Code), illegal employment (Article 170/a of the Criminal Code), falsification of documents (Article 186 of the Criminal Code), laundering of the proceeds of a criminal act or criminal activity (Article 287 of the Criminal Code).

In our opinion, the criminal offense of income concealment, when committed by a commercial company, has a specific subject, since it can only be committed by the legal representative of this company and specifically by the administrator of the company. However, the accurate identification of the person responsible for committing this criminal act is made after we are acquainted with the statutory organization of the commercial company, which allows us to determine the persons who have the power and their duties, within the framework of which they can commit that punishable behavior by criminal provision. Even when the company is administered by an administrative council and no delegated administrators have been appointed, all of them are criminally responsible. Nonetheless, each of them may prove non-involvement in it and thus the absence of guilt (Kurti, 2016). Most of the problems in identifying the active subject of this criminal offense arise in large companies, where special advisors are delegated functions in the field of tax obligations.

Nowadays, it is very important to work to increase people's desire to pay taxes and levies. For this reason, many countries have pursued such a policy centered on increasing the level of controls and implementing penalties against the authors of tax evasion. However, it is impossible for these measures to be effectively implemented. On the other hand, there is a widely spread expression in criminal law: the punishment must fit the criminal act. Moreover, increasing penalties and the high level of control would cause a high cost for both governments and individuals. Perhaps the best policy is a pragmatic one, which accepts that tax evasion cannot and should not be eliminated. It is also important to note another fact: since tax affects the economic and financial power of the taxpayer, it is necessary that it always be determined in a lawful, fair, and accurate manner. Therefore, the issue is that under no circumstances in determining taxes should misunderstandings of arbitrariness by tax authorities be allowed.

3. Economic Analysis of Tax Evasion

Tax evasion highly favors commercial companies as it gives them the opportunity to create large sums of money which can help them during the exercise of their commercial activity, securing a dominant position in the market. Although this is a benefit for the company itself and its partners, in our opinion, it is detrimental to the economic development of a state. Among the negative consequences that tax evasion can have on the economy, the most significant are: *Reduction in tax and levy collection,* *negatively impacting the limitation of public services.* We can mention many public services that the state must provide for its citizens but let us focus only on healthcare services. According to statistical data, the approximate value of tax evasion in Albania is equal to 47,265,937 dollars every year: of these, 43,486,591 dollars every year is the amount that the state budget loses from the evasion of commercial companies and 3,779,347 dollars every year is the amount that the state budget loses from the evasion of individuals. This sum constitutes about 7.81% of the budget allocated each year for the health system and simultaneously amounts to the annual wage of 8,260 nurses (The State of Tax Justice 2020). If these funds were declared in the state budget, there would be more revenue available to increase the number of doctors and nurses to better cope with the problems facing the healthcare system, *Creation of uncontrolled revenue sources in society.* In this case, it refers to those funds which can finance other criminal activities, such as drug trafficking or arms trafficking or can be used in the process of laundering dirty money which is extremely harmful to the economy (Barresi, 2007). Referring to the data extracted from the Financial Intelligence Agency, from 2019 to 2023, a total of 38 suspected cases of money laundering have been identified, where the criminal act of origin is related to income concealment. Money laundering is an illegal process characterized by the illegality of the revenues generated by criminal activities and aims primarily to cover the illegal origin of these revenues (Zoppei, 2016). One of the identified methods to carry out the money laundering process is the creation of commercial companies. The circulation of capital of illegal origin in the legal economy, through the creation of commercial companies, can affect the latter in several key aspects: Disruption of competition rules. For this, let us imagine a construction company inclined to launder the money of organized crime that corruptly steals tenders or buys construction permits by dressing the money to be produced from the construction act in the guise of legality; Businesses of money launderers have liquidity “at low cost”, thus avoiding the risk of bankruptcy or financial difficulties of the enterprise. This would lead to market destabilization which would be dominated by “criminal” businesses that would act in the form of monopolies or oligopolies which are harmful to the economy; Even in this case, legitimate businesses would tend to follow non-competitive economic policies, in contrast to the laws of free trade and with negative consequences for the economy of a state; An increase in clashes between illegal businesses and legitimate ones would be noted. The latter would be victims of financial crises (difficulties in securing liquidity), of fines or of illegal competition and it is known that crime in general and especially economic crime is a major problem for the economy, *Causing a feeling of non-respect and non-implementation of the law*. In fact, it might happen that regular commercial companies, paying tax obligations, when they notice that their competitors are strengthened due to tax evasion, will seek to do the same. The increase in this feeling would lead to very negative consequences for the economy of a specific state, therefore it is necessary to take the necessary measures to control, identify, and punish the illegal behaviors of tax evasion committed by commercial companies; *Evasion affects the accuracy of macro-economic statistics and the undertaking of* *appropriate economic and social policies*. Every government bases its economic and social policy precisely on state budget revenues. The more accurate these statistics and the less tax evasion there is, the more efficient the government's decision-making for the implementation of appropriate policies for economic and social development; *Evasion is also costly in the context of its prevention: measuring tax evasion is very difficult*. Where there is a lot of tax evasion, a very repressive criminal policy is required but cannot be afforded by the financial resources available, this is also because of the revenues missing in the budget because of evasion. For the state to recover economically, it must first fight tax evasion, but for this, it needs to take on debt also because it must also think about the "bread" of its citizens.

4. Motives that Complicate the Fight Against Tax Evasion

One of the criminological theories that best explains the causes of the commission of criminal acts of an economic nature is the economic theory of criminal behavior (Kurti, 2022). The greatest importance of this theory lies in the fact that it serves as a guide for drafting an effective criminal policy in the fight against economic crime. In other words, it is possible to influence the commission of criminal behaviors if, through certain policies, the costs and benefits that are at the foundation of these behaviors are influenced (Becker, 1974). This theory explains another characteristic of criminal behavior, the case when a specific subject decides to distribute its resources either in the commission of lawful acts or in the commission of unlawful acts. As for tax evasion, there are subjects that declare all their income and there are others who declare nothing. On the other hand, there exists a wide range of subjects that declare only a part of their income. These latter behave in this way because they have decided to distribute the resources of their income in the commission of various activities, thus distributing and reducing in this way the risk of the portfolio they possess. Even in this case, these subjects make a rational choice that considers all the penalties that will be taken in cases of discovery of various violations, including the case of tax evasion: the smaller the penalty or the smaller the probability of detection of evasion, the greater the evasion.

The question that is most often raised concerns the determination of the motives that complicate the fight against tax evasion. According to the supporters of this theory, there are several motives, specifically: *The activities undertaken to combat tax evasion are costly and the resources in possession of the competent authorities are limited.* We can say that to identify all those people who hide their income, we need to increase the number of controllers, but they are costly. The economic theory allows us to clarify this fact by using the theory of marginal utility according to which "each additional unit purchased will increase marginal utility if the benefits that will be had from the purchase of this additional unit will be greater than the costs that must be incurred; since benefits always tend to decrease and costs always tend to increase, this action will reach its optimal dimension when the benefits from the additional unit will be equal to the cost of that unit"; These conclusions can also be applied in the case of combating tax evasion: for example, every cent spent on increasing the fight against tax evasion (hiring more tax officers, police, and magistrates; spending to equip oneself with more effective tools to conduct investigations) will undoubtedly produce a greater additional benefit, but on the other hand, we must keep in mind that with the increase in expenditures, the additional benefits tend to decrease until a point comes when it is no longer advantageous to increase expenditures (Martucci, 2006). *The policies pursued to combat tax evasion are the result of decisions of a series of public authorities* and therefore the arrival point of a long chain composed of several decision-making subjects that interact with each other: the voters, the parliament, the government, the competent offices, the subjects responsible for implementing in everyday life the activities foreseen during the drafting of these policies. Each of these subjects follows its own objectives, which often may be in contrast with the objectives of the other subjects. A branch of economics called "game theory" can analyze such situations where the choice is the result of an interaction like the one described above. Even if each of the subjects involved in the game engages in making rational choices, this does not mean that the final decision (the result of the game) will always be efficient. In such a case, supporters of this theory call this outcome "coordination bankruptcy" (Kurti, 2024). For example, let's consider that voters, based on the information they have, have concluded that the state of tax evasion in the country is at alarming levels. On the other hand, this erroneous perception of the situation by the voter's contrasts with the real state of tax evasion reflected in the official statistics. In this case, the parliament and government, in line with their objectives, will seek to respond to the concerns of the voters by excessively inflating expenditures for the implementation of activities to combat tax evasion beyond what would be necessary for such a situation:*Sometimes during the implementation of the policies pursued to combat tax evasion, the various authorities charged with advancing this fight may encounter the continuous pressure of interested subjects that these policies should not be implemented.* Such pressures, if on the one hand, become an obstacle to combatting crime, on the other hand, constitute in themselves an illegal activity and in the specific case, we are dealing with the criminal act of corruption.

5. Conclusion

Income concealment has chain effects throughout the socio-economic life of a country because it simultaneously damages the normal functioning of tax systems in many aspects. Such behavior, being illegal, not only reduces state revenues but also limits the ability of the countries in question to balance inequalities through taxes. Tax systems exert a considerable influence on the dynamics of state building and the perception of social incomes and power relationships. Alongside generating revenue, taxes and levies involve the redistribution of incomes and assets, and the curbing of undesirable social behaviors.

Tax evasion is costly in the framework of implementing preventive measures. The real determination of its dimensions is extremely difficult. Various states have created different policies to measure the extent and dimensions of tax evasion as this would make its control easier and more predictable. However, since people are always motivated towards the concealment of taxable incomes, over time even the methods they use to "cheat" the state become more complicated. One of the most used methods to measure the value of tax evasion is based on the information brought by checks carried out by employees of the tax administration during the exercise of their functions. From these data, the "true" incomes of individuals, both physical and legal entities, are determined, thus making an approximate calculation of tax evasion possible. This method has several downsides because these controls do not manage to determine undeclared incomes, leading to serious errors in measuring tax evasion. Tax evasion significantly increases the possibility of committing money laundering, and both these criminal acts have extremely negative impacts on economic growth. Tax evasion fosters a feeling of disrespect and non-implementation of the law, affects the accuracy of macro-economic statistics, and the undertaking of appropriate economic and social policies.

Another important point, which should be given priority by our legislator, relates to the punishment of tax evasion in commercial entities. Statistically, most of the evasion in any state is carried out by commercial companies, and to curb this phenomenon to some extent, besides interventions of an economic nature, it is important to specifically penalize this type of tax evasion in the Criminal Code. In our opinion, punishing with heavy fines, equal to or slightly greater than the value of tax evasion, could help in preventing this illegal behavior.

Competent authorities should begin to conduct parallel financial investigations related to criminal acts in the field of taxes and levies. It should also include in the category of criminal acts for which Law No. 10192 dated December 3, 2009, "*On the prevention and striking of organized crime, trafficking, and corruption through preventive measures against property*", as amended, applies, even the criminal acts related to taxes and levies (articles 180-182/a of the Criminal Code).

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