

# Fighting Against Tax Evasion – A Comparative Approach Between Romania, Hungary and Anglo-Saxon Countries

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## Abstract

*The coronavirus pandemic, which began in 2019, has caused a global health crisis as well as an economic downturn worldwide. National budgets and economic operators both have suffered significant revenues losses, while expenditure has been multiplied, due to the overfunding of the health sector and the recovery of businesses that have gone bankrupt, to save jobs and to create new ones. Optimal tax systems could play a major role in reducing the increased public deficits. It is essential to the states to collect and redistribute taxes in an effective and fair way. Consequently, one of the main tasks of the tax authorities is to step up in the fight against tax fraud and curb the black economy. The study presents the fight against tax evasion from Romanian and Hungarian perspectives. In the third part of the work, the authors discuss some Anglo-Saxon tools used to combat tax fraud, providing an opportunity to compare them with the Central and Eastern-European approaches.*

**Keywords:** *taxation, tax fraud, tax evasion, tax compliance, public administration, digitalization, digital tools, high court decision, jurisdiction practices.*

## I. An introduction to tax fraud and tax evasion

Tax evasion appears in every country – which has tax systems – at different levels. According to Anthony D. Williams, this behavior is necessarily and undoubtedly linked to tax norms and can only be eliminated by the illusion of tax-exempt societies<sup>4</sup>. We can find tax fraud and tax evasion or tax avoidance in every social class or group, and in every economic system. However, until the second half of the twentieth century, relatively little attention was paid to the problem. Major synthesis works on tax theory, such as Richard Gude's monograph on personal income taxation<sup>5</sup> and Musgrave's *Theory of Public Money*, did not consider the issue of tax evasion as a relevant topic. A significant change occurred in the 1980s, when tax avoidance, tax planning have gained attention of legislators and international institutions. According

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<sup>4</sup> A.D. Williams, *Trends in Anti-Avoidance*, Bulletin of IBFD XI-XII, 1996, pp. 502-503.

<sup>5</sup> R. Gude, *The Individual Income Tax Washington*, 1964, D.C. The Brookings Institution.

to professor Uckmar we can find the reason for this perspective change in the economic recession<sup>6</sup>. During the banking and stock market crisis of 2008<sup>7</sup> or the pandemic of 2019, taxpayers contributions decreased and their willingness to pay taxes deteriorated. Governments forced to compensate the rising expenditure side by borrowing, and without new types of public revenue, it is essential to ensure a more efficient use of existing taxes. With reference Professor Uckmar's work, economic recession is repeating itself from time to time, as evidenced by the events of 2008 and the current coronavirus situation.

In addition to the above, it is important to note that the efficiency of tax administration is significantly linked to the new international dimension of tax compliance. National governments need to understand the increasing internationalization activities of businesses and individuals. Taxpayers have recognized the wider economic opportunities of globalization. The establishment of regional confederations, trade and economic treaty systems allowed the free movement of capital, labor and goods. The situation has created new challenges for national tax systems. Many authors have recognized that the development of industry and trade has opened up new opportunities for tax evasion through transfer fees, capital and profit shifting<sup>8</sup>. This process has facilitated the concealment of economic events and in parallel has made tax authorities enforcement procedures more difficult<sup>9</sup>. Nowadays, one of the biggest challenges for tax authorities is to detect and tax the wealth transferred to offshore centers<sup>10</sup> and to force multinational companies to proportionally pay taxes regarding their economic activities. The globalized economy and technological innovation mean new, modern tax collection opportunities for countries and, at the same time, new tax avoidance solutions for tax evaders.

According to the complicated financial web of tax matters, it is easy to think that the abovementioned issues only matter for tax professionals and not for ordinary citizens. However, a newly published Eurobarometer survey shows otherwise<sup>11</sup>. Three quarters of Europeans believe that the fight against tax fraud should be the third most important priority for the European Union, after the fight against terrorism and the reduction of unemployment.

## II. Tax evasion in Hungary and Romania

The transformation process of Central and Eastern-European economies from socialist into capitalist economies has had serious consequences for their tax systems.

<sup>6</sup> V. Uckmar, *General Report of ITA*, 1994, pp. 11-15.

<sup>7</sup> See further Z. Bujtár, *Reregulation of securitization in the United States and the European Union after the subprime crisis of 2007-2009*, in *Economics & Working Capital* 1-2/2020, pp. 34-40.

<sup>8</sup> See eg. E. Saez, G. Zucman, *The Triumph of Injustice: How the Rich Dodge Taxes and How to Make Them Pay*, New York, 2020; or G. Zucman, *The Hidden Wealth of Nations: The Scourge of Tax Havens* University of Chicago Press, 2016; see further T. Piketty, *Capital in the Twenty-First Century*, Harvard University Press, 2017.

<sup>9</sup> D.-G. Mockherje, *Incentives and Institutional Reform in Tax Enforcement*, Delhi, 1998, pp. 246-248.

<sup>10</sup> B. Layman, *Az Offshore halála* [The death of the Offshore], Libri, 2011.

<sup>11</sup> <https://www.europarl.europa.eu/news/hu/headlines/priorities/adomegallapitasok/20160707STO36204/az-europaiak-haromnegyede-komolyabb-unios-fellepest-var-az-adocsalas-ellen> (accessed on 14.11.2021).

Although, complex economic, political and social circumstances slowed down the implementation of desired changes<sup>12</sup>. The two ex-socialist countries under review have been permanently reforming their tax systems<sup>13</sup> to meet the upcoming challenges of international tax competition, the expectations of European Union and the constant changing fiscal and social needs. They have, tried to meet these demands with different approaches and different tax measures.

### ***II.1. Tax evasion in Hungary since the change of regime***

Hungary was ahead of other Central and Eastern-European former socialist countries in the reforming of the tax system and catching up with western standards, as the 1987/88 tax reform implemented the modern forms of value-added tax, personal income tax and corporate income tax in the Hungarian tax system. These steps have given Hungary a 10-15 years advantage in establishing a “Western-European” economic structure and legal framework. It was the first comprehensive tax reform in Central and Eastern-Europe, and perhaps the most significant too. The depth and pace of the changes and the newly introduced tax norms created significant challenges for both individuals and entities in Hungary. One of these challenges was to understand the forms of tax avoidance that have come with the capitalist market economy and to develop a sufficiently effective institutional and legislative environment. In the early 1990s, there were various legal and illegal forms of tax evasion, ranging from tax planning – tax optimization to deliberate tax evasion – that were not defined comprehensively by Hungarian legislation. We must notice that 30 years later there is still no consistent separation of the various types of behavior. The new Criminal Code has abolished the separate offence of tax fraud and incorporated the concept into the collective offence of budget fraud<sup>14</sup>. In our point of view, the mentioned solution makes it more difficult to assess the legal status of the various types of conduct and thus makes it harder to combat tax fraud successfully. Following the change of regime, there were many compliance issues, which were not adequately addressed by the 1988 tax reform.

The low level of Hungarian compliance has greatly affected by the facts that the tax office was initially unprepared, had a small staff and technical knowledge, and for a few years, until the entry into force of Act XCI of 1990 on the Rules of Taxation, it was unable to build an independent and efficient administrative system. At the beginning of the 1990s, the revenue shifted from taxation was estimated an amount of HUF 200-400 billion, which was the 2.4% of Gross Domestic Product in 1990. Tax experts recognized that creating special rules are fundamental to combat tax evasion. The Act 1991 on Tax Administration has already contained more efficient provisions and safeguards against tax evasion<sup>15</sup>.

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<sup>12</sup> V. Tanzi, *Tax reform and the move to a Market Economy: Overview of the Issues*, in OECD, *The Role of Tax Reform in Central and Eastern European Economies*, Paris, 1991, pp. 19-34.

<sup>13</sup> Tax reform is when the changes significantly alter the tax system, including the tax code or the tax administration as a whole, and create new or significantly modified elements that are able to operate more efficiently and create more favorable conditions for taxpayers. Tax reform can be a combination of improving the functioning of the public finance system, increasing tax revenues and raising the level of compliance. However, a change implemented solely for the sake of fiscal surplus is not a tax reform, but a tax increase. Likewise, a continuous, small annual adjustment of the tax structure and a shift in the tax burden cannot be called a reform.

<sup>14</sup> Act C of 2012 on the Criminal Code 396. § (1) Budget fraud.

<sup>15</sup> G. Földes, *Pénzügyi Jog* [Financial Law], 1999, p. 115.

The lack of precise normative definitions of tax evasion activities has slowed down the fight against tax fraud. In its decision 21/1993 (IV.2.) the Hungarian Constitutional Court found the obligation to declare wealth and assets unconstitutional and abandoned it, this step worsened the efficiency of tax compliance. Thus, it became more difficult to conduct asset and wealth investigations, which process is considered one of the most successful tools in the fight against tax evasion in many countries like Greece, Romania and Brazil.

The European Union reports from the mid-2010s have described Hungary as a tax haven because of the favorable mix of tax incentives and state aids provided to multinational companies. We must highlight that in the last decade tax competition has increased globally for winning multinational firms to settle down in the countries. Regarding this, a large number of states try to simplify their tax systems and reduce their tax rates. The result of the mentioned situation can be seen in the current Hungarian corporate tax law. In 2017, the 30 largest foreign companies in Hungary paid only 3.2% tax on their profits<sup>16</sup>. The gap between the nominal and the effective corporate tax rate has been opened wide for businesses that make maximum use of the possibilities offered by the underlying tax regulations. We can conclude that foreign companies have a competitive advantage over domestic players in the capital-poor SME sector<sup>17</sup>.

We can state that several major public finance reforms have been implemented in the past 30 years of Hungarian economic policy. These include the tax reforms in 1987-1988 linked to the change of regime, the "Bokros package" in 1995 and the tax changes implemented by the second Orbán government in 2011. We can conclude that the Hungarian tax system, like in many other countries in the region, has been in permanent reform since 1988. In our point of view, the level of tax compliance has been significantly undermined by the inconsistent and rapidly changing tax law environment and the absence of transparency in the system and the norms as well. However, in the last few years we found some promising efforts from the legislator.

The public finance reform in 2010 aimed to make the tax system more efficient, more customer-friendly and to reduce the tax burden. The complex tax measures have broaden the tax base without raising taxes, while other elements reduced the size of the black economy by restricting the amount of illegal gains. The common feature of all measures was that they relied on a greater cooperation from taxpayer side. The legislator also simplified tax administration and broadened the audit database through technical means, without imposing a significant additional burden on taxpayers. In other words, most of the changes were focused on providing a more accurate and real-time picture, building up a new database to access information in order to understand the real processes of the economy. A basic condition for well-functioning tax administration is that business activity does not become a "black box". It can be stated that any tool that improves transparency also improves the efficiency of the tax administration.

The package of measures included, among others, the obligation to use online cash registers, the introduction of reverse value-added tax payments, the targeted reduction of value-added tax rates, the creation of EKÁER and, last but not least, the introduction of

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<sup>16</sup> P. Bucsky, *Magyarország lassan tényleg adóparadicsom lesz* [Hungary is slowly really looking for a tax haven], available at G7 <https://g7.hu/kozelet/20190122/magyarorszag-lassan-tenyleg-adoparadicsom-lesz/> (accessed on 22.10.2019).

<sup>17</sup> Z. Bujtár, *Az értékpapírosítás* [The securitization], University of Pécs, Állam- és Jogtudományi Kar, 2021, pp. 231-234.

online invoicing. We can see that a number of measures took with regard to value-added tax transactions. The main reason behind this is that a significant proportion of tax fraud in EU countries takes place in this tax. In 2017, the value-added tax loss at EU level was estimated at an amount of EUR 137 billion. The biggest value-added tax shortfall in 2017 was in Romania, where 36% of the expected value-added tax revenue did not reach the central budget<sup>18</sup>.

A major step forward in the fight against value-added tax evasion was the innovation of EKÁER<sup>19</sup>. It is a technical system for monitoring, controlling and registering the movement of goods, launched and operated by the Hungarian Tax Authority in 2015. The primary objective of EKÁER was reducing the number of abuses and value-added tax fraud related to the transport of goods. The system covers transactions between Member States and the first domestic movement of goods for supply to a non-end user, as well as the advance electronic recording of these statutory data by the tax authorities and the declaration of the transport. The efficient operation of EKÁER<sup>20</sup> is supported by the so-called HU-GO camera system. Two countries have already introduced a similar electronic tool after recognized the success of the Hungarian system. In Poland, a roadside inspection system called SENT, following the Hungarian model, operating since 1 May 2017<sup>21</sup>. Slovakia introduced the technology in 2018. In addition, several countries have indicated that they are monitoring the experience of the Hungarian operation and are interested in its introduction.

The legislator's main objective was to establish a customer-friendly tax authority, and the introduction of the e-personal income tax system was a successful step forward in this direction. As a result, in the tax year of 2019, 5.0613 million taxpayers used the digital tax returns prepared by the Hungarian Tax Authority. 3.3273 million taxpayers accepted their pre-prepared returns without any changes. The next goal of the Hungarian Tax Authority is to help companies preparing their tax returns and by 2021 all invoices issued will be connected to the tax authority's central digital system<sup>22</sup>.

The authors welcome the Hungarian tax provisions made in recent years, because there was a significant reduction in income taxes and, in parallel an improvement in tax compliance too. Hungary ranked first in 2017 and third in 2016 and 2018 among the OECD's tax cut leaders. With a 13% value-added tax gap, Hungary holds a strong second place in the region, ahead of only Austria (7%)<sup>23</sup>.

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<sup>18</sup> C. Szilovics, *Hatékony eszközök az adócsalás elleni küzdelemben* [Effective tools in the fight against tax fraud] in: C. Szilovics, Z. Bujtár, B. Ferencz, B. Breszkovics, Al.R. Szívós (eds.), *Gazdaság és punzutyúk a 21. Százaban II, Konferenciakötet* [Economy and punches in the 21st century II, Conference], *Business and Economy in the 21st Century II*, Conference Proceedings, Pécsi Tudományegyetem Állam – és Jogtudományi Kar, 2020, pp. 39-51, p. 13.

<sup>19</sup> L. Varga, *Az EKÁER helyszíni ellenőrzésének tapasztalatai*, Adóvilág XX [Experiences of the on-site inspection of EKÁER, Tax World XX], 2016, pp. 29-31; see also I. Magyar, *Százmilliárdos adócsökkentés jövőre. VM interjú* [One hundred billion tax cuts next year. VM interview], available at <https://magyaridok.hu/gazdasag/szazmilliardos-adocsokkent-es-jovore-2456239/> (accessed 22.10.2018).

<sup>20</sup> C. Szilovics, *On a new tool to combat tax evasion*, *Journal of Eastern-European Criminal Law* no. 1/2019, pp. 34-43, p. 10.

<sup>21</sup> Poland has introduced a system called SENT, modeled after the Hungarian EKÁER. Information available at <http://www.mkfe.hu/hu/mediamenu/hirek/aktualis-hrek/148-kulfoldi-hrek/8173-lengyelorszag-c3%A1g-bevezeti-a-sent-nev%C5%B1-rendszert,-a-magyar-ekaer-mint%C3%A1j%C3%A1ra.html> (accessed on 14.02.2020).

<sup>22</sup> <http://www.e-adotanacsadas.com/930-mi-varhato-a-magyar-adozasban-mutatjuk-a-negy-legfontosabb-iranyt.html> (accessed on 09.11.2021).

<sup>23</sup> Hungary is no longer the country of VAT fraudsters. Available: [https://piacesprofit.hu/kkv\\_cegblog/mar-nem-magyarorszag-az-afacsalog-orszaga/](https://piacesprofit.hu/kkv_cegblog/mar-nem-magyarorszag-az-afacsalog-orszaga/) (accessed on 12. 01. 2020).

The Hungarian government radically changed the legal definition of tax fraud in 2012. It was a part of the fighting against the black economy. From 1 July 2013, the National Assembly amended the legal definition of tax fraud, which had been settled in the Criminal Code for 30 years and incorporated it into a new comprehensive definition of budget fraud. As a result, the acts previously covered by 7 separate offences can be assessed by the law enforcement authorities under a single offence. Under the current legislation, the criminal offence of budget fraud can be divided into three basic cases: budget fraud in the strict sense, tax evasion on excise goods and administrative budget fraud. With this regulatory solution, the norm combines a wide range of offences, from misappropriation of budget funds to false tax declarations and concealment of an important fact concerning budget revenue.

Compared to the previous act, the legislator's change of approach was also noticeable with regard to the result of the offence. Whereas previously the reduction of tax revenue was the result of the offence, the new legislation focuses on the damage caused to the budget. The aim of the modification is to protect the financial interests of a broader legal object, the budget, and through it the whole community, by creating a *delictum complexum*. An examination of recent case law shows that the legislator has not achieved this objective. The legal unity that has been created has created a number of doctrinal and legal difficulties in the work of adjudication and investigation. One of these is the problem of determining the date of completion of the unit of offence when assessing the unity of the law. In this respect, the Supreme Court of Hungary stated in a decision from 2018: "In the case of budget fraud, the date of indictment concludes the unit of offence, so that all the factual elements of the offence committed during the period up to that date fall within the scope of the unit of offence, regardless of whether they were committed for different types of taxes and contributions, as well as if they would not constitute an offence individually"<sup>24</sup>. The biggest problem with this reasoning was that offences discovered after indictment, which are typically repeat offences, can only be protected by criminal law through retrial. The issues places a significant and unjustified burden on the investigating authority, the prosecution and the court system. An equally difficult task in the new regulatory environment is the interpretation of the grounds for non-continuity and decriminalization. In assessing the effectiveness of the new legislation, it can be said that, although it has remedied many of the shortcomings of the previous legislation, its unusual legal technicalities have created new problems which need to be amended and clarified in the future in order to ensure practical application.

## ***II.2. The situation of tax evasion in Romania during the period of regime change and in the following decades***

Romania's tax law is similar in both its principles and its detailed solutions to those of other CEE countries. In terms of compliance, most estimates put the share of the black economy at 50-60% of GDP from the period of regime change until the early 2000s. Among the Central European countries, Romania had the highest rates of inflation and corruption, and the shortest period of tax compliance. After the change of regime, the extraordinary size of the black economy became one of the biggest problems facing lawmakers. Up until the early 2000s, the European Union and the International Monetary Fund (IMF) regularly drew attention to the size of the Romanian black

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<sup>24</sup> BH2018.162.

economy and called for greater predictability and transparency in the business world. The country has tried to make progress in the fight against corruption and the black economy through a series of innovations. One element of this was Romania's ratification in 2004 of the 1999 Strasbourg Criminal Law Convention on Corruption, together with its Protocol<sup>25</sup>. The fight against tax evasion was helped by the amendment of the Penal Code, which redefined the offences of bribery and influence peddling.

The most important instrument in the fight against corruption was created when the National Anti-Corruption Directorate was established, a specialized prosecution office specialized in the fight against corruption at the middle and top levels<sup>26</sup>. Its activities have proved successful, as confirmed by the statistics of recent years and the international repercussions of its activities<sup>27</sup>. Investigations into corruption or maladministration are, as a rule, conducted by the National Anticorruption Directorate (DNA) within the Prosecutor General's Office. Investigation, detection and collection of evidence is the responsibility of the investigative authority, but all participants in the proceedings have the opportunity to submit evidence during the proceedings.

A priority in the EU's accession negotiations with Romania in 2004 was to improve the fight against tax evasion and avoidance, in parallel with the reform of fiscal policy and the fiscal system. High tax rates and inefficient tax collection machinery have contributed greatly to the growth of the black economy<sup>28</sup>. A number of other factors contributed to the spread of tax evasion, including the tax law, which was characterized by loopholes, inconsistencies, ambiguities and lack of stability, and the late emergence of the anti-avoidance law<sup>29, 30</sup>. According to the literature, the average level of tax evasion in developing countries is equivalent to 25% of annual budgets. The Romanian tax system in the mid-1990s suffered from inefficiencies in tax administration, similar to other Central European countries' models, which it has not been able to overcome successfully. By the 2005 tax reform, all the major central tax types applied in European countries had been introduced, accompanied by low tax rates, but the level of efficiency of the tax administration was weak. Economic policy makers have sought to apply a mosaic of tax legislation, using legal instruments, tax instruments and tax mixes already successfully applied in other countries. In order to increase efficiency, they created a system that resembled both the Hungarian and Croatian structures emphasizing consumption taxes, while at the same time adopting elements of the Slovak tax system, such as the single rate for personal income tax and corporate tax and drawing on the Austrian example for property taxation.

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<sup>25</sup> ETS 191.

<sup>26</sup> P. Novoszáth, *There is no other way for society than fairness and respect for the law. Evaluation of the Romanian Anti-Corruption Agency*, in *Citizen's Review* 2015, <https://polgariszemle.hu/archivum/101-2015-december-11-evfolyam-4-6-szam/gazdasagpolitika-jegybankpolitika-allami-ellenorzes/714-nincs-mas-ut-a-tarsadalom-szamara-mint-a-korrektseg-es-a-toervenytisztlet-a-roman-korruptcioellenes-uegyneokseg-mukoedesenek-ertekelese>.

<sup>27</sup> *Ibidem*.

<sup>28</sup> L.-L. Albu, *Estimating the Size of Underground Economy in Romania* in *The Economics of Transition*, June 1, 2004, p. 3. Available at SSRN: <https://ssrn.com/abstract=1569577> or <http://dx.doi.org/10.2139/ssrn.1569577>.

<sup>29</sup> D. David, D. Pojar, *Approaches Regarding The Tax Evasion In Romania*, 2011, p. 378, [https://www.researchgate.net/publication/227462770\\_APPROACHES\\_REGARDING\\_THE\\_TAX\\_EVASI\\_ON\\_IN\\_ROMANIA](https://www.researchgate.net/publication/227462770_APPROACHES_REGARDING_THE_TAX_EVASI_ON_IN_ROMANIA).

<sup>30</sup> D. Clocotici, Gh. Gheorghiu, *Dolul, fraudă și evaziunea fiscală* [Deception, fraud and tax evasion], Ed. Lumina Lex, Bucharest, 1996, p. 56.

In order to regulate tax evasion, Law 87/1994 was enacted in 1994<sup>31</sup>, Article 1 of which defines tax evasion as follows: 'Tax evasion is the evasion, in whole or in part, by any means, of Romanian and foreign natural and legal persons from paying taxes, duties and other public charges, including local budget payments and state social insurance funds'. This wording protected a broader range of public-law liabilities than Article 310 of the old Hungarian Criminal Code. Romanian jurisprudence and legal literature recognizes several variants of tax evasion and distinguishes between legal and illegal tax evasion. In general, tax evasion (*evaziune fiscală*) is the case where a taxpayer evades paying tax. However, not all behaviour is considered to be a breach of the law when taking advantage of the legal possibilities. Tax evasion is illegal and punishable when the law is knowingly broken (*evaziune fiscală frauduloasă*). The legal assessment of this can be twofold. In the milder cases it is considered a misdemeanour – *contravenție* – and in the more serious cases listed above it is considered a felony (*infracțiune*).

The initial ad hoc, inconsistent and opaque tax structure was completely rewritten and redefined by the 2003 Tax Code. It was for this reason, and in preparation for EU accession, that the Romanian legislature adopted Tax Law 571/2003, which, in an unusual solution, regulated the whole of the previously highly fragmented tax system in a unified structure. Interestingly, in stark contrast to the other CEE countries, only Romania has seen a decline in its tax revenue-to-GDP ratio in the first ten years after EU accession. The country's public tax revenue is still below the EU average by more than 10%<sup>32</sup>. Bulk of the Romanian state's tax revenues is levied on consumption and labor, while taxes on capital and property are negligible<sup>33</sup>.

A more precise formulation of the criminalization of tax evasion was undertaken by Law 241/2005. Under the umbrella term of tax fraud, the legislator criminalized several types of conduct that jeopardizes the collection, assessment and payment of tax revenues. Law no. 241/2005 on the prevention and combating of tax evasion set out in detail the conduct that falls within the definition of tax evasion. Article 9 of the Act. Article 9 of the Penal Code provides that the following acts committed with the purpose of evading tax obligations constitute a criminal offence of tax fraud and are punishable by imprisonment for a term of 2 to 8 years and deprivation of certain rights: concealment of an object or source liable to tax or duty, total or partial failure to record commercial operations or income in accounting documents or other legal documents, recording in accounting documents or other documents of expenses relating to operations which are not real or other fictitious operations, damaging, destroying or concealing the memory of accounting documents, tariff clocks or electronic tax cash registers or other recording devices, double-entry bookkeeping by means of transcripts or other recording devices, evasion of financial, tax or customs controls by failing to declare the principal or secondary establishment of controlled persons, by declaring a fictitious establishment or by inaccurately declaring it, by competent bodies – bodies responsible for carrying out financial, tax or customs controls in accordance with the

<sup>31</sup> V. Panescu, *Evaziunea fiscală* [Tax evasion], 1999, Bucharest, p. 3.

<sup>32</sup> See <https://data.worldbank.org/indicator/GC.TAX.TOTL.GD.ZS> 6.06.2021. Also see C. Ban, Al. Rusu, *Romania's Eak Fiscal State. What explains it and what can (still) be done about it. Economy and Finance*, 2019, <http://library.fes.de/pdf-files/bueros/bukarest/15914.pdf> (accessed on 13.05.2021).

<sup>33</sup> See A.-M. Izvoranu, H.-C. Calin, *Taxation System in Romania and in the European Union*, 2018, [https://www.researchgate.net/publication/324756496\\_TAXATION\\_SYSTEM\\_IN\\_ROMANIA\\_AND\\_IN\\_THE\\_EUROPEAN\\_UNION](https://www.researchgate.net/publication/324756496_TAXATION_SYSTEM_IN_ROMANIA_AND_IN_THE_EUROPEAN_UNION) (accessed on 26.09.2020) and C. Ban, Al. Rusu, cited.



law, and by the judicial police, criminal investigation bodies"<sup>34</sup>. The range of the penalty is adapted to the extent of the damage caused in this respect being similar to the Hungarian legislation. The legislator's intention was that tax evasion should be considered to be the deliberate or negligent breach of documentary obligations resulting in the loss or destruction of supporting documents. Obstructing official controls was also considered to be tax fraud. The legislator has made the offenders of tax fraud liable to criminal prosecution only. However, behind this apparently strict system, which appears to be dogmatically more elaborate than in Hungary, there is still a poorly paid tax administration with a weak technical base and low public morale.

The new regulatory attitude has resulted in a significant increase in the number and proportion of white-collar crimes detected. The penalties set out in the criminal law have been further tightened. Following a 2013 amendment to the law, the maximum statutory penalty for tax evasion is increased to five years if the damage is equal to or exceeds €100,000 and to seven years if the damage exceeds €500,000 in national currency. The effectiveness of controls and investigations has also been enhanced by the fact that, in addition to the law enforcement authorities (police) and the courts, the relevant authorities for investigation and sentencing in the Romanian legal system always include the prosecution with special expertise in cases against white-collar criminals.

Despite the implementation of tax and criminal law reforms, experts say that the black economy and tax evasion rates have not fallen as much as expected<sup>35</sup>. Sometimes increasing, sometimes decreasing tax burdens and constantly changing tax obligations have made the Romanian tax system unpredictable for economic operators, which has undermined compliance<sup>36</sup>. Even in 2012, Romania and Bulgaria were the worst performers in the EU in terms of the share of the black economy and tax evasion. In nominal terms, this meant that 29.6% of gross domestic product generated no revenue for the state. By contrast, in the same period, the black economy in the Western model state, Austria, was estimated at only 7.9%. It is telling that the Romanian tax revenue in 2017 was only 15.42% of GDP, in line with the French statistics of 1926 and the US statistics of 1942<sup>37</sup>. Tax evasion and the flight of the wealth generated from the country is largely due to the multinational companies established in Romania, whose activities are nonetheless essential to survive in a competitive economy. According to some estimates, in their absence exports would fall by 70% and GDP by 30%. This is why the legislator grants disproportionate tax breaks and exemptions to foreign capital. The<sup>38</sup> country is committed to minimizing the tax burden on multinationals and to treating their transfer pricing practices leniently<sup>39</sup>.

Due to legislative changes and social pressure, there has been a marked increase in the internal control activities of parent companies in the Romanian subsidiaries of multinational companies, indicating that the zero tolerance of law enforcement agencies

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<sup>34</sup> See <https://www.monitoruloficial.ro/actimp/hu/0272.pdf>. Also see Dr. Edit Szentpáli Balláné, *The characteristics of deceptive behavior in budget fraud*, PhD thesis, 2020, University of Debrecen, Faculty of Law, pp. 75-77.

<sup>35</sup> Quoted by E-Népújság.ro, published in the daily newspaper Gândul, 27.12.2012.

<sup>36</sup> See C. Szilovics, *Experiences of tax credits in some Central European countries in the last two decades*, PTE ÁJK, JURA no. 1/2018, pp. 142-160.

<sup>37</sup> C. Ban, A. Rusu, cited, p. 4.

<sup>38</sup> *Ibidem*.

<sup>39</sup> B. Dick, M. Rafferty, D. Wigan, *Capital unchained: finance, intangible assets and the double life of capital in the offshore world*, Review of International Political Economy 24(1)/2017, pp. 56-86.

in relation to economic crime has been understood by company managers. Companies have adapted their own internal regulations to promote transparent and orderly operations. The companies have made a clear statement of their distance from any criminal activities and from the persons who have committed criminal activities on behalf of the company. The only way for companies to be exempted from criminal prosecution is for them to take an active part in the investigation of the crimes by carrying out detailed investigations. Individuals who "voluntarily" disclose the commission of crimes and make a detailed confession before the authorities discover the crime are called "whistle-blowers". There are various options available to the authorities to protect whistle-blowers, but they are not specialized for economic crime, but are applied according to general rules. They can either protect repentant offenders or their relatives or keep their identity secret during proceedings.

On the positive side, Romania has achieved outstanding results in the period 2004-2017 in simplifying tax administration and reducing the number of hours needed to fulfil certain tax obligations<sup>40</sup>, thanks to the possibilities offered by digitalization, including for employment taxes and VAT<sup>41</sup>.

### III. Lessons from regulatory practice in the Anglo-Saxon countries

In addition to the practice of the two Central and Eastern European countries, it may be useful to briefly review the main instruments of the anti-fraud legal systems of some Anglo-Saxon countries. It may be very instructive to note that the Anglo-Saxon countries also use solutions to combat tax fraud that differ from continental law. The most striking difference is in the United Kingdom, where there is no general anti-avoidance measure. In this legal system, the role of judicial legislation is paramount, and the emphasis is on analogy and infringement of the spirit of the law, and on interpretation of legislative intent, as opposed to the normative approach of continental law. Such a picture of the British approach emerged from the work of Bracewell – Millnes, Sawyer, Jones. These authors argued that the English approach, which does not make a significant distinction between culpable and intentional tax evasion and the exploitation of loopholes in the law, is outdated. "There appears to be no substantive or procedural distinction between tax avoidance and tax planning, on the principle that the economic consequences are the same. Tax evasion is generally referred to as tax avoidance, which implies the nature of a deliberate crime, since the purpose of tax laws is to collect taxes and not to conceal them". In this spirit, the British attitude is that any way of avoiding the law is illegal. The<sup>42</sup> fact is that it is for Parliament to lay down clear and unambiguous rules and for the courts to interpret them. There is, however, a somewhat contradictory view, expressed by Lord Tromlin, that 'every man has a right to arrange his affairs so that his taxes may be less than they otherwise would be under the proper law'<sup>43</sup>, but that he can only achieve this by legal means.

<sup>40</sup> C. Ban, A. Rusu, cited, p. 21.

<sup>41</sup> See for example F. Gherghel, *Aspects regarding electronically supplied services*, in WTS CEE, Taxbridge no. 2/2019, *Going Digital: Trends in Taxation and Administration in Central and Eastern Europe*, p. 11, [https://wts.com/wts.com/publications/cee-tax-bridge/2019/wts-cee-tax-bridge-2019\\_2.pdf](https://wts.com/wts.com/publications/cee-tax-bridge/2019/wts-cee-tax-bridge-2019_2.pdf) (accessed on 5.12.2021).

<sup>42</sup> V. Uckmar, cited, pp. 5-6.

<sup>43</sup> (1936) 19 Tax Cases ("TC") 490.

The question is for the courts to decide when considering the legal transaction and their role is therefore enhanced. In *A. Ramsay (W. T.) Limited v IRC*, the House of Lords agreed with the decision of the court when it considered the transaction not only as a whole but also in its steps. The court stated that the legality of the sham steps, which had no independent economic justification, could not be recognized. In so ruling, the Ramsay case inadvertently provided a model for the fight against continental tax evasion. According to Chelvathurai<sup>44</sup>, 4,000 tax cases in England were settled as a result of the Ramsay precedent and the Treasury collected £1.2 million in tax. This judicial decision has transformed tax jurisprudence and reduced the scope for tax evasion by providing a general rule for the interpretation of a legal transaction.

### ***III.1. Australia***

The Australian tax system is considered one of the most modern in the world. The main aim of Australian lawmakers is to separate the inadvertent and deliberate modes of tax evasion. A strict distinction is made between the two. The legislator clearly intended to punish only intentional tax evasion. Innocent conduct should not be penalized even if it is otherwise by its nature a reduction in tax liability.

In Australia, very early on, in 1936, the Australian Income Tax Act (ITA) provided for the minimization of unacceptable tax burdens in section 260. This, unlike the English legislation, was specifically designed to prevent deliberate tax evasion. Section 260 stated that it was prohibited to ascribe to any law a meaning other than that which it did not expressly state, and therefore prohibited to interpret it expansively if it would result in a reduction in public revenue. The purpose of this legislation was to provide an objective and uniform interpretation of the concept of tax evasion in order to ensure that taxpayers behave appropriately in critical situations. A public finance policy must be implemented that is capable of cracking down on contrived and devious tax avoidance practices. Of course, this has never included regular commercial transactions where taxpayers legitimately take advantage of the opportunities to settle their affairs".

The Australian jurisprudence on tax fraud is characterized by the fact that, as in English jurisprudence, the courts have emphasized the primacy of substance over form<sup>45</sup>. The Australian courts have always placed a premium on the precise definition of the purpose of the transaction, following the English model of "substance before form". At the same time, they have taken into account English case law, and have applied a strict interpretation of the wording of the Act, from *Ramsay (W. T.) Limited v IRC*<sup>46</sup> to *Fuzniss v Davis*<sup>47</sup>, or *Westminster*<sup>48</sup>. Australian jurisprudence is also characterized by a strictness of judgement that exceeds that of other Anglo-Saxon countries. "They take the view that, interpreted literally, their anti-avoidance action extends their investigation to any transaction that may have resulted in a reduction in the taxpayer's income"<sup>49</sup>. Numerous rulings in Australian case law have developed the distinction between legal tax reduction and what is defined in law as tax evasion. This

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<sup>44</sup> S.I. Chelvathurai, *Tax Avoidance, Tax Evasion and the Underground Economy*, Bulletin of IBFD XII, 1990, p. 594.

<sup>45</sup> C. Szilovics, *Fraud and compliance in tax law*, Gondolat Publishing House, 2003, p. 49.

<sup>46</sup> (1981) 54 (T.C.) 101.

<sup>47</sup> (1984) 55 (T.C.) 324.

<sup>48</sup> (1963) 19 (T.C.) 490.

<sup>49</sup> S.I. Chelvathurai, cited, p. 595.

judicial attitude has a strong tradition in Australia. As long ago as the 1926 *Wilson or Chamberi Co.* case, the Supreme Court held that tax evasion could be established by "any trick, artifice or sham." In *Isaacs* I Rio's view, anyone who withheld a compulsory payment without any reasonable excuse or legal basis was cheating the payment. The avoidance may appear to be a simple consequence of the practice of minimizing the tax burden, although the mere failure to pay may be inadvertent or by mistake. But the concept of fraud always involves more than simple omission. The Australian judges have taken into account the 1949 decision in *Denver Chemical Manufacturing v. Commissioner of Taxation (Denver)*<sup>50</sup>, in which Judge Dixon himself stated that it was unwise and impractical to define tax evasion in terms of its multifaceted nature. Nevertheless, he himself defined the essence of tax evasion in terms of reprehensible conduct or knowing omission, which is punishable. The Anglo-Saxon Federal Courts and the Supreme Courts have accepted that intentional conduct or at least omission is necessary to establish tax evasion. In *Barri*, Judge Williams explained that the omission of income to minimize the tax burden must be intentional in order to establish tax evasion. However, in *Brambles Holding Ltd v AITR*, Judge Barwick, in the words of the English Lord Tromlin, held that a taxpayer has the right to choose a genuine transaction which will result in him obtaining the benefit of the tax law, i.e. minimizing his tax. Despite this, section 260 of the ITA proved to be quite ineffective and by the 1970s Australian taxpayers had developed a number of sophisticated tax avoidance schemes. In response to this, the Government introduced an anti-avoidance measure (IVA) in 1981-82 to replace ITA section 280. The legislation created a strict regime in which, on a literal interpretation, a transfer of an income-producing property between husband and wife could be considered invalid. The penalty under the norm is also strict and the taxpayer is liable to pay double the amount of tax foregone in addition to the tax foregone. In addition, in December 1980, the Tax Crimes Act was passed, which criminalized a number of tax deduction practices and made the assistance of experts an offence. The so-called general provisions continued to apply, nullifying and thus rendering invalid any transaction whose purpose, directly or indirectly, was to evade tax.

In 2008, the Australian Taxation Office (ATO) issued a practical guide<sup>51</sup> for authorities and taxpayers, setting out the elements of the distinction between tax avoidance and tax evasion. This provides guidance for both parties and is used by auditors during audits. The guide is regularly reviewed, supplemented and updated. The Practical Guide sets out that the definition of tax avoidance is inevitable for tax audits and legal consequences. The definition of tax avoidance is based on the expectation that the taxpayer has engaged in conduct (omission) that is attributable to the taxpayer. The concept of omission, or reprehensible conduct, lies halfway between culpable conduct and intentional conduct. Most often, taxpayers engage in this conduct by making an incorrect or erroneous declaration or return. Tax audits must factually examine whether the taxpayer has acted with due diligence. Adequacy must be equated with the care and responsibility expected of a 'diligent person'. Under Australian tax policy and tax law, tax liabilities can only be investigated by the authorities within a specified time limit. This is generally between 2 and 4 years for income tax. However, in certain cases the authorities may also examine tax liabilities retrospectively for an

<sup>50</sup> *Denver Chemical Manufacturing v. Commissioner of Taxation* (1949) 79 CLR 296 at 313.

<sup>51</sup> "Fraud or Evasion" PS LA 2008/6.

unlimited period. Examples include tax evasion or tax fraud in the context of fringe benefits or income tax. Another interesting provision is that tax evasion or tax fraud can only be established during a tax audit by a senior auditor or a senior auditor. This is obviously intended to ensure that the finding is thorough, justified and professional. If the investigation reveals significant tax evasion or tax evasion with a future risk, the tax auditor, in addition to the Tax Counsel Network (TCN), must notify the National Fraud or Evasion Advisory Panel (NAFEP), which will examine whether the finding was objective and fair. The suspected tax fraud is investigated by a panel of at least 3 senior officials. Australian tax law recognizes and regulates aggressive tax planning and treats any transaction as such if there is little or no economic rationale behind the business actions.

### ***III.2. New Zealand***

New Zealand has a highly developed and modern tax system. The New Zealand Tax Authority regularly issues information leaflets to taxpayers setting out the principles on which the process, which they describe as a 'red code', can be based. If these conditions are met, a thorough and detailed tax audit can certainly be initiated<sup>52</sup>. The authority has made clear in its information to clients that tax evasion and tax fraud often go hand in hand with money laundering. Illegally obtained income is also taxable, so money laundering also involves clarifying the origin of assets. In general, it is established that operations to launder the proceeds of tax evasion can implement classic money laundering techniques. Clients will carry out sham transactions such as the inclusion of tax havens in business transactions or the performance of acts incompatible with sound management. The essence of tax avoidance is defined as the failure of a taxpayer to meet his or her actual tax obligations. This can take two forms, either by not recording all of his income or by understating income by fictitiously increasing expenses and deducting the amount from income. Tax evasion is defined as a scheme whereby the offender clearly obtains unlawful income. This is considered to be the case where taxpayers file fictitious returns, prepare false invoices or vouchers and record their tax liabilities on that basis, or claim benefits on the basis of false information. As there are some sources of income that are tax exempt, e.g. casinos, horse racing, gifts, tax evaders prefer to claim that their money comes from these transactions. It is extremely interesting that the tax authorities' information note gives detailed examples of schemes and signals to which the authorities react immediately. In the case of cash predominant services (hairdresser, beauty salon etc.) it is highly suspicious if the private and business bank accounts are with the same bank and card payments are made to the business account, while cash deposits to this account are negligible, while cash deposits to the private bank account are continuous. The guidance also states that in this case, the authority will assume that the cash flow is not reported by the customer as a business flow. It also specifies which states are considered tax havens and lists them (e.g. Bahamas, Samoa, Cayman Islands, MAN Islands etc.) For information and service purposes, it also specifies which transactions trigger an immediate Code Red. These are transactions involving states that function as tax havens or complex and unusual economic transactions that cannot be explained economically. These might include the use of a private bank account for business transactions. In order to

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<sup>52</sup> New Zealand Government, *Tax evasion, tax fraud and money laundering*, Inland Revenue, IR1061 | July 2019, [www.ird.govt.nz](http://www.ird.govt.nz).

ensure transparent and traceable payments, the PAYE system was introduced in 2019, which is derived from an English acronym [Pay As You Earn (PAYE)].

## IV. Conclusions

In conclusion, the two countries have made progress in the fight against tax evasion over the last two decades, mainly as a result of the opportunities offered by digitalization. However, insufficient attention has been paid to the incorporation of Western principles in tax legislation and to the development of judicial enforcement. The results achieved and the whitening of the economy are due to the simple technical tools presented in the study, which have long been used in other Western countries. We are not talking about an internal strengthening of the level of compliance or a significant reduction in taxes, but 'only' about a well thought-out electronic improvement in the control of the tax administration. A more effective solution would seem to be the introduction of new taxes aimed at a slight improvement in the performance of the tax administration and the modernization of technical conditions, rather than a substantial overhaul of the tax system. In many ways, a well-prepared, well-paid, adequately staffed and politically neutral tax administration can achieve more than any reform. A segmented tax administration that is aware of and responsive to the taxpayers' tax activity characteristics is the key to success. The new approach needs to focus not only on developing digital tools but also on developing a collaborative tax administration model. Digitalization can also be used to better engage with customers, to listen to taxpayer opinions, to monitor the media and to process information from both domestic and international peer organizations.

In terms of legal standards, both countries have successfully caught up, although the concepts of tax fraud, tax evasion, tax avoidance and tax optimization have still not been consistently contrasted in Hungarian legislation. However, changing the rules is not enough if the financial literacy of the population is low, as illustrated by the brokerage scandals and pyramid schemes of recent decades and the high level of corruption in the legal practice<sup>53</sup>. It is encouraging that the development of financial awareness has been increasingly emphasized in recent years, but programs, organizations and educational materials dealing with this issue should discuss the importance of taxation and compliance with the law much more strongly.

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<sup>53</sup> L. Kőhalmi, *Korrupciósage in Ungarn* [Corruption in Hungary] in C. Szilovics, Z. Bujtár, B. Ferencz, B. Breszkovics, A.R. Szívós (eds.), *Gazdag es pegnzugyek a 21.Szazadban II. Konferenciakotet* [Rich and money in the 21st century II. Conference volume] *Business and Economy in the 21st Century*. Conference Proceedings, Pécsi Tudományegyetem, Állam – és Jogtudományi Kar, pp. 182-193, p. 12. Also see L. Kőhalmi, *Fehérgalléros bűnözés, gazdasági bűnözés, korrupciós bűnözés* [White-collar crime, economic crime, corruption crime] in T.A. Barabás (ed.) *Alkalmazott kriminológia* [Applied Criminology], Ludovika Egyetemi Kiadó, pp. 431-444, p. 14.

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