THE IMPACT OF THE INSTABILITY AND UNPREDICTABILITY OF THE TAX ENVIRONMENT ON THE ECONOMY

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Abstract
The tax rate on the profits of Romanian companies is among the lowest, but the value of foreign investments does not reflect this. Thus, we deduce that there are other factors that influence foreign investments. Our hypothesis is that such factors are the complexity of tax legislation (i.e. bureaucracy), instability and unpredictability of the fiscal environment etc. In this research we will investigate the impact of the instability and the unpredictability of the fiscal environment on the Romanian economy. By instability, we mean frequent changes to regulations; by unpredictability we understand the lack of coherence of the changes. According to the literature, the effort made by a company to ensure regulatory compliance is, generally, greater than the benefits generated by a reduced tax rate. The research question is: "In an economic environment with a rapid evolution and a dependence on international financial markets, how do companies identify, quantify and diminish the fiscal risk generated by the unpredictability and instability of the tax environment?" The research is based on a questionnaire, which was distributed to persons attending specialized courses. The target group consists of financial and accounting professionals and tax professionals. The results are: the instability and the unpredictability of the fiscal environment adversely affect the decisions of the investors, thus the economy.

Keywords: *taxation, tax uncertainty, investment, fiscal risk, tax compliance,*

Clasificare JEL : *M40, M41*

1. Introduction and context of the study

Tax burden represents a significant factor taken into account when an investing decision is made. However, tax burden is not generated only by tax rates and tax incentives, but also by tax uncertainty.

In the report issued by the OECD and IMF [7], upon the request of the G20 Leaders at the Summit in Hangzhou, China on September 2016, it was highlighted that there is a risk that tax uncertainty is discouraging investment.

In this paper we discussed the impact of instability and unpredictability of the tax environment. We used survey methodology to understand tax and accounting professionals' opinions on this matter.

We consider tax uncertainty caused by the instability and unpredictability of the tax environment is affecting companies and tax and accounting professionals from Romania. Tax compliance of the taxpayer is also affected by the complexity of the tax code and the frequent changes of the legislation.

The results of our survey show that because of instability and unpredictability of the tax environment, it is important and recommended to have a tax professional within the company or externalized that assures tax compliance for the company. However, in many cases accounting department is insuring the tax function as well.

Our respondents, mainly accounting professionals, consider necessary to participate in tax legislation courses, in order to deal with the instability and unpredictability of the tax environment and to be able to assure tax compliance for their companies.

The paper is structured as follows. The first section represents a review of the literature in the area of tax uncertainty. In the second part we described the methodology used in the paper. The third section covers the main results of the survey and in the last part we presented our conclusion.

2. Literature review

Though the effects of tax uncertainty on investments are ambiguous in theory, in this section of the paper we have summarized the researchers' findings in this area.

Tax uncertainty is generated by many factors, such as complexity of the legislation, unpredictability of the tax environment and is affecting both taxpayers and governments. Though there is no irrefutable evidence of the impact of tax uncertainty on investment and economy, most researchers agree upon the common sources of tax uncertainty. These sources are presented below in Table 1.

Table 1. Tax uncertainty - sources and recommendations

Paper	Sources of tax uncertainty	Recommendations to improve tax certainty
Tax Uncertainty: Economic Evidence and Policy Responses; March 2017	At domestic level: - complexity of the fiscal code; - frequent tax changes; - inconsistent and unpredictable treatment by the tax authorities; - the flaws of the process of pursuing a tax reform/change; At international level: - differences in the tax systems; - different interpretation of the tax systems.	At domestic level: - simplification of the tax rules and tax compliance system; - a structured approach in the development of tax policy. At international level: - cooperation between countries by having common approaches in fighting tax evasion; - agreement between countries on a fair distribution of tax revenues for cross-border transactions
Tax certainty - IMF/OECD Report for the G20 Finance Ministers, March 2017	From businesses perspective: - issues related to tax administration, such as: bureaucracy to comply with legislation, inconsistent treatment; - inconsistent approaches of tax authorities in application of international tax standards; - issues related to dispute resolution mechanism, such as timescale. From tax administrations perspective: - taxpayer behaviour, as result of aggresive tax planning and lack of cooperation; - complexity of the tax legislation; - frequency of legislative changes; - lenghty court procedures.	- reducing complexity of the legislation; - improving tax policy design; - increasing consistency and predictability by tax authorities; - having effective dispute resolution mechanism; - cooperation and coordination between countries.

Source: Authors' own research

Though theoretical literature concludes that the impact of tax uncertainty on investment is unclear, according to Devereux [2], uncertainty of the effective tax rate on profit is the third most important factor in terms of investment and location decisions.

At a domestic level, tax uncertainty is generated mainly by the complexity of the tax code and the differences in interpretation tax law according to Ernesto Zangari [3].

Tax uncertainty is affecting taxpayers' behavior as well. James et. al [5] has examined through laboratory experiments the effects of uncertainty on taxpayer behavior and his results indicate that uncertainty lowers compliance if taxpayers perceive they receive a public good in exchange for their tax payments, while uncertainty increases compliance if taxpayers receive nothing for their payments.

In order to increase tax certainty and tax compliance, governments have implemented measures such as issuing public and private rulings, to clarify the legislation in a specific area. Private rulings are issued upon taxpayers' request and are often subject to a fee. However, Diller et. al [6] states that taxpayers that face tax uncertainty often do not use advance tax rulings.

Ernesto Zangari [3] state that tax certainty could be improved through a proper planning of the tax reforms and changes, as well as through a clear communication of their content and timing. They found that one of the main sources of tax uncertainty is the flawed tax policy process.

At an international level, tax uncertainty is generated mainly from the differences in tax systems.

Due to differences in the tax systems between countries, corporations tend to complicate their business structure with the scope of tax avoidance. Thus, tax uncertainty generated at an international level by the differences in tax systems is affecting both taxpayers as well as governments.

Tax treaties, known also as double taxation agreements, have the purpose of eliminating double taxation of the same revenue or transaction, by setting out rules regarding the allocation of taxes on cross-border transactions. Because sometimes the parties of these agreements can have different opinion on interpretation of the rules in a specific area, the dispute can be resolve through a mutual agreement procedure (MAP). In the Tax Administration Series issued by OECD [8] it was reported that at the end of 2015, the number of open MAP cases from OECD countries was 6.176, compared to 5.429 from 2014. Therefore, we can conclude that MAP is a procedure not yet effective in decreasing tax uncertainty.

While there are significant research papers that conclude that tax uncertainty has a negative impact on investment, there are also researchers that do not agree with this theory. Bohm and Funke [4] have demonstrated by using models of irreversible investment under uncertainty that private investment spending will not necessarily increase by reducing tax policy uncertainty.

We consider that Romania's tax uncertainty derives from frequent changes of the tax code and the overall process of tax reforms and changes – its unpredictability and instability, and is affecting tax compliance.

3. Methodology

For this paper we used survey method. The survey was distributed to tax and accounting professionals, and to business owners, during tax legislation courses. 78 respondents completed the survey, from 12 different counties. The data was collected in the period October – December 2018 during three seminars.

Table 2 presents the counties of the business headquarters of the respondents. Most responses were received from Cluj and Bucharest.

Table 1. Number of respondents from each county

The county where your business is based is:	
Alba	1
Bihor	2
Bistrita nasaud	1
Bucuresti	24
Cluj	31
Constanta	1
Dambovita	3
Ilfov	3
Maramures	7
Mures	1
Satu-mare	2
Sibiu	1
Suceava	1
Total	78

Source: Authors' own research

As shown in Table 3, most of respondents have more than 10 years of working experience in tax and/or accounting area.

Table 3. Number of respondents by seniority

Seniority in financial accounting and/or tax (in number of years):	
5-10 years	12
more than 10 years	60
under 5 years	6
Total	78

Source: Authors' own research

To understand the scale of the business involved, respondents were asked to provide the number of the employees of the company they work for, the 2017 turnover of the business and 2017 value of the total assets. As Tables 4 shows, the respondents cover all types of companies, from small enterprises to medium and large companies.

Table 4. Number of respondents by business size

The number of employees in your business is:		The turnover of your business in 2017 (in euro) was:		Total of your business' assets in 2017 was (in Euro):	
0 employees	1	between 0 and 100.000	14	between 0 and 100.000	16
between 1 and 9	12	between 100.001 and 5.000.000	32	between 100.001 and 5.000.000	29
between 10 and 250	37	more than 5.000.001	29	more than 5.000.000	24
more than 250	27	no response	3	no response	9
no response	1				
Total	78	Total	78	Total	78

Source: Authors' own research

4. Results and discussions

The purpose of the survey was to discuss how companies diminish the fiscal risk generated by the unpredictability and instability of the tax environment.

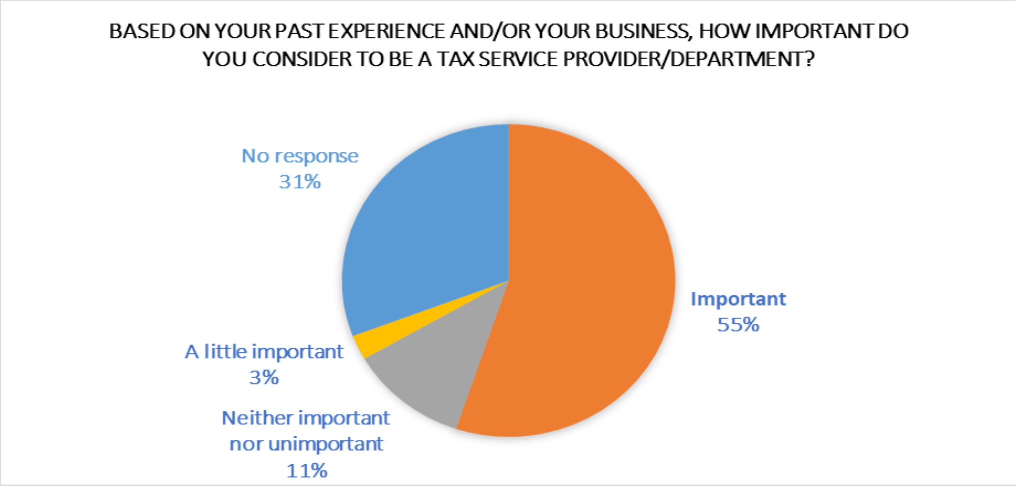
Unpredictability and instability of the tax environment has been an increasing issue in Romania, with approximately 120 articles of the Tax Code being changed/completed by 8 normative acts in just the first three months of 2018, according to a press release published by the National Council of Small and Medium-Sized Private Enterprises in Romania [1].

The business environment as well as tax practitioners have requested the government an open and transparent decision-making process, an impact analysis of proposed legislation on SMEs before the date of entering into force of the changes, to provide a stable, predictable and reasonable legal framework, and to restore investor confidence.

Based on our experience, due to tax uncertainty companies have difficulties with tax compliance. In order to decrease the fiscal risk generated by the unpredictability of the tax environment, taxpayers use tax services providers - either specialized companies or tax professionals (individuals). Yet, 87.18% of our respondents stated that there is no tax function separately from the financial-accounting department within the companies they worked for. In the same time, most of our respondents (58.97%) consider that such a function won't be created during the next 3 to 5 years for their companies neither internally nor externally to the organization.

We consider that a tax specialist is important for any business that operates in an environment with high tax uncertainty and 55% of the responders agree.

Figure 1 – The importance of a tax service provider/department



Source: Authors' own research

However, 12.82% of the respondents employed in companies in which such a function exists could not identify any value added brought by the function for the entity.

Within our sample the persons employed in the tax department were mostly accountants (41.02%), followed by persons with another economic specialization (10.26%) and persons who are specialized in something else than economics (2.56%).

One of the cases in which a separate tax function can help the company is during the control from a state authority. 38.46% of our sample did not have any control during the last five years. The rest of the respondents had a background check. From tax authorities (26.92% of the entire sample), an audit regarding only the direct taxes (15.38%) or an audit regarding only the indirect taxes (19.23%). Most of the tax audits did not lead to any penalties (57.69%). In the case of 20.51% of the sample the penalties were less than 50,000 lei (approximately 12,000 euro).

According to 55% of the responders, when they had the opportunity to make an investment, they had taken into account the fiscal burden associated with the investment. However, most of the respondents (48.71%) did not discuss with anybody before deciding to make an investment. The rest of them made the decision after receiving the advice of an auditor (19.23%), lawyer (14.10%) or tax consultant (17.95%). It is interesting to notice that none of our respondents discussed with any representative of the state before making an investment. This could be a proof of the lack of trust of the respondents in the Romanian state authorities.

Most of the respondents (58.97%) did not use the due diligence before making an investment in Romania. It would be interesting for a future analyses to discuss whether it is the cost of a due diligence that makes investors not use this service or there are other factors to take into account. The ones who used it had to support in general a cost of 1-3% of the total value of the investment.

It results from the first part of our questionnaire that in most of the cases our sample companies do not have any separate tax function. This activity is covered in general by the accountants. Yet, as there is an important body of changes at the level of the tax regulations, we assume that the accountants need to train themselves continuously.

Thus, the majority of our respondents (91.03%) have professional training whenever they consider it necessary. 88.46% of our respondents state that they attend the lectures in order to be informed on the changes and the suggestions of changes in regulations. We notice that this preparation does not come as an obligation enforced by the Romanian professional organizations (as only 10.26% attend lectures in order to comply with the rules of these organizations), but as a necessity felt by the respondents. This is an interesting result because there are three professional organizations in Romania and each of them has requirements regarding the professional training. These requirements are synthesized in table 5.

Table 5. The requirements of the professional organizations regarding the training per year

Organization	**Number of compulsory hours of training per year for active members**
CECCAR – The body of expert and licensed accountants of Romania	40
CAFR – Chamber of Financial Auditors of Romania	40
CCF – The Chamber of Tax Consultants	30

Source: Authors' own research

Most of the respondents (39.74%) have more than 20 hours of training per year. The rest of them have less than 10 hours (20.51%) or between 10 and 20 hours (30.77%). From the point of view of our respondents, the optimum length of a training seminar is of one day (64.10%). Also, the preferred seminars are classic (requiring the presence of the trainee in the lecture room), with 66 answers out of the 92. They are followed by the lectures which involve the study of some materials with the possibility to address questions to a specialist, with 15 answers. Our respondents prefer the lectures organized in a conference room in the city they live in (60 answers out of 77).

The respondents attend lectures in various areas. We obtained in total 130 answers regarding this question. Most of the lectures are in the tax domain (66 answers), followed by financial accounting (44 answers), management accounting and IFRS (with ten answers each). We notice that even though most of our respondents are accountants, they prefer to attend tax lectures. We assume that this is because the changes related with the taxes are more frequent than the ones related to accounting. Also, accounting operations are in general repetitive.

We obtained 98 answers regarding the supplier of professional training lectures. Out of these, 59 answers were allocated to the specialized Romanian companies. This is well above the lectures provided by the professional organizations (only 28 answers), the state entities (9 answers) or a foreign company (such as ACCA) – only two answers.

The benefits the respondents expect after attending a professional training lecture are mostly on the short term (76.92 of the respondents).

Most of our respondents (43.59%) allocate 500 – 1,000 euro or less than 500 euro for the professional training (33.33%).

5. Conclusions

Tax uncertainty has affected Romanian entities in many ways. The lack of predictability of the tax environment and the flaws in the decision-making process is making difficult for companies to make a budget and to forecast their future results. Tax changes are made by the government without prior impact analyses on the companies.

Though based on our results tax function is considered important and should be performed by specialized personnel as tax environment is instable and unpredictable, in many cases this function is performed by the accounting department.

It would be interesting to discuss why the tax function is not separated by the accounting department. It is because investors consider accounting professionals should be able to assure tax compliance as well or because they consider the cost of such a separate function would be higher than its benefits?

Another reason for which representatives of the companies involved in the survey are not interested in having a separate function within the company or externalized that assures tax compliance could be the lack of tax audits.

In order to cope with the instability and unpredictability of the tax environment, accounting and tax professionals attend tax legislation lectures on a regular basis.

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