

Aspects of Control Over tax-shelter

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Abstract. Tax fairness is becoming increasingly important to the economies of the EU countries. The main topic on the agenda of the sitting state and government heads in May 2013 was the policy of taxation. Identified as priority in the conclusions are the measures for control over tax frauds, tax sheltering and aggressive tax planning. The aim is to protect the public interest by ensuring "confidence in taxation fairness and effectiveness".¹

The article considers the aspects of tax-sheltering control by finding the influence of different factors: normative terms, documentary frauds; the presence of virtual economy, quasi-markets.

Keywords: virtual taxation control, fiscal control, virtual currency.

JEL: G 28, H39

I. INTRODUCTION

The importance of the topic for tax-shelter control is underlined by the finding that "the EU loses 1 trillion (one thousand billion EUR) from tax evasion by individuals and companies every year". This equals to the 7-year budget of the Community.² "In our country "900 Bulgarians have sheltered income of 450 BGN" in the first eight months of 2012"³.

The main categories to be investigated are: tax evasion, tax-shelters and aggressive tax planning. Tax evasion is expressed by all illegal acts committed against the tax (fiscal) system. The term tax shelter has the broadest meaning. It includes these two concepts as taxes are sheltered through fraud, as well as through "legal" methods. It involves taking advantage of: gaps in current legislation, collisions between legal rules, abiding the law, but the abuse of the "essence" (context) of the current regulations. Aggressive tax planning is carried out by qualified professionals (often accountants) aiming to reduce the taxable value and move the profits of corporations in offshore accounts, parent companies or branches (subsidiaries), related individuals or individuals without income or property.

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¹ <http://www.european-council.europa.eu/>, last updated on 15.10.2013

² See <http://www.investor.bg/evropa/>, last updated on 15.10.2013 - statement of the European Internal Market Commissioner Michel Barnier in an interview for the French newspaper Monde.

³ See <http://www.on-parliament.com/>, last updated on 15.10.2013

II. ASPECTS OF TAX-SHELTERING CONTROL ACCORDING TO THE NORMATIVE TERMS.

Legal environment affects the methods of tax fraud and sheltering prevention. The regulatory framework defines the requirements that must comply with the activities of the taxpayers. The divergent and frequently changed laws discourage revenue authorities, which affects their efficiency. The national legislation includes a number of fiscal discipline recommendations from the EU. An adopted directive 2011/85/EC applies to the budget frame of the member countries and introduces requirements for the "national numerical fiscal rules."⁴

The National Reform Program of Bulgaria for 2013 contains the recommendation of the EU Council of 9 July 2013 on the establishment of "an independent body whose task is to oversee fiscal policy and prepare analysis and advice."⁵ In connection to this has been prepared a bill for establishment of a Fiscal Council and the decision to create a "Fiscal investigations" administration.⁶

The scale of financial machinations affecting tax collection requires fiscal control. The latter includes elements of tax, insurance, customs, banking and exchange control. Its legal basis is contained in the special substantive acts and norms of financial law. Financial control is designed to collect statutory budget revenues and aims to implement the fiscal policy. Despite the danger of penalty perjury, tax sheltering is still a widespread activity. On May 21, 2013 the members of the European Parliament adopted a resolution expressing the desire that "the member states would unite and reduce by half the gap of 1 trillion annually uncollected taxes by 2020."⁷ The reasoning for it states that "the scale of cross-border tax fraud is scandalous and the one-sided measures are not a sufficient counteraction," said Mojca Kekush (Slovenia), reporter for tax evasion.⁸ It is stated that tax evasion has led to losses amounting to 125 billion euro in developing countries - twice more than the international assistance they received.

⁴ See <http://eur-lex.europa.eu/>, last updated on 15.10.2013

⁵ See <http://www.minfin.bg/bg/page/578>, last updated on 15.10.2013

⁶ See <http://www.nap.bg/>, last updated on 15.10.2013

⁷ See <http://www.europarl.europa.eu/news/>, last updated on 15.10.2013

⁸ Same link, a statement of Mojca Kleva Kekush (S&D, Slovenia), reporter for tax evasion.



In addition to providing revenue to the budget, fiscal control also influences society's sense of justice. In terms of global financial crisis there is a shortage of financial resources for the implementation of social services (health, education, disaster, etc.) and for administrative activities. Despite the reduction in cost, there are activities which must be performed. They have to be paid by each equal standing citizen. In cases of tax evasion and sheltering the costs of social activities are covered by those who pay their taxes in good faith. Thus, correct taxpayers compensate for the concealed taxes by taking up additional taxes. One pointed possible measure is introducing a "tax mole" that will facilitate the coordination in the EU and provide information for each country's tax reductions and increases.⁹

In that context is adopted the Directive on administrative cooperation (DAC), including through automatic information exchange (AIE). It provides that from 2015 the member states to automatically exchange information on the following income and capital categories: employment; management remuneration, life insurance products that are not covered by other directives; pensions and ownership of real estate or retention income.

It is planned to expand the scope of the automatic information exchange by 2017 for a more efficient cooperation between the member states of the EU. The plan will include the following positions: dividends; investment income; other financial income; balance of accounts.¹⁰

Priority areas in the fight against tax fraud and shelters are also: taxation of savings income; fight against VAT fraud and transfer of profits; counteraction of aggressive tax planning; eliminating harmful tax measures; fight against money laundering - in the EU and globally; challenges connected with taxation in the digital economy.¹¹

These legal provisions aim the unified information gathering on the underlying tax events. The automated data exchange leads the fiscal control bodies to complex measures against tax frauds and sheltering.

III. ASPECTS OF CONTROL OVER TAX-SHELTERING, ACCORDING TO DOCUMENTARY FRAUD.

A document is a subject of research in various sciences - economic, legal, informational, technical, historical, etc. Legal opinions on the document are the narrowest in scope. They are used for the legal doctrine's objective and are based on written recording. Archival science document study science,

etc., have a broader scope. They define documents as "all written or in any other way recorded pieces of information, meant to be communicated and passed through space and/or time."¹²

Legal interpretation is based on the Supreme Court's practice including the adopted in 1982 decision that "a subject of documentary crime is a document which is a specific written statement containing facts or circumstances or allegations of the existence of facts or circumstances of legal significance."¹³

The European Parliament has decided that the document is an information carrying medium, whether in paper, electronic form or as a sound, visual or multimedia recording.¹⁴

All the facts and circumstances relevant to the tax process can be proven on the basis of a document. The development of communication technologies leads to changes in fixing, storing, transferring and data using methods. There are various ways for manipulating the document content relevant for taxation of liable for tax individuals. To cut down tax fraud and sheltering we need to draw up the prerequisites and conditions favouring indecorous document. Revenue authorities must identify the specific dimensions of the consequences of a criminal creation, use, concealment or destruction of documents.

1. Large number and variety of documents. The variety of documents can be systematized by the following criteria: document content; its origin; information storage medium; degree of summing up; processing of documents; publisher; authorship; document compliance with reality; specific characteristics of the issuing entity; degree of completeness; the document's role in legal proceedings; belonging to the issuer of the document; usage period; level of typification, complexity of the information contained; urgency to create the documents, degree of obligation, confidentiality, etc.

2. Replacing paper with electronic document meeting the requirements of the Law for the Electronic Document and Electronic Signature. This is an innovation enabling the creation, storage and use of a larger volume of documents. It facilitates quicker document flowchart and *approval of new standards for control of documents*. Documents created through optical technology can be combined in a system whose control is based on the characteristics of electronic documents: *the unification of the details; opportunity to select the data; typifying of documents; options for integration into virtual folders, libraries, systems*

⁹ Same link, the proposal is included in the resolution on the annual report on taxation.

¹⁰ Council Conclusions on tax fraud and tax evasion from May 14, 2013 (Doc.9549/13 - FISC 94 - ECOFIN 353).

¹¹ See <http://www.european-council.europa.eu/>, last updated on 15.10.2013

¹² Анчова, К., Барутчийски, С., Бурмова, М., Крайчева, Ж. И Др. Речник на българската архивна терминология, със съответствия на руски, френски, английски и немски език. Варна, ВСУ "Черноризец Храбър", 2002 г., с. 33.

¹³ Decree № 3 from 1982 at the Plenum of the supreme court.

¹⁴ See Regulation (EC) № 1049/2001 of the European Parliament and the Council of Europe, Art. 3, letter "a".

for information, etc. A major problem of tax inspection bodies is that it is easy to manipulate the data contained in electronic documents. The possibility to partially report money received from sales through a computer program is a prerequisite for tax fraud.

3. Identification of forged documents in the tax control process can be studied in two main aspects: *factors* favouring the falsification and *control procedures* for finding manipulated documents.

4. Determining the tax documents authentic and accurate requires knowledge of falsification methods. Control procedures are designed to establish: the document's nature; its contents; type of offense; method of forging; type and degree of damages / losses; user of the false document; responsible individual; ways for prevention, etc.

Control procedures for finding manipulated documents can be classified into the following areas:

1. Revenue authorities control the type of the illegal act under which they can determine:

2. Physical document forgery - when a document that doesn't come from the person considered to be the author of the will expressed. In this case there needs to be found whether the true author has been concealed or another specific person is being imitated.

3. Intellectual document forgery (a false document) - when the contents of the document present false facts.

4. Control the methods for implementation of the forgery :

5. Making a false document - describing facts and circumstances relevant to the tax process for the first time.

6. Altering the contents of an existing document - when the document is genuine, but the data it contains is manipulated in order to lower the tax amount.

7. Check the user of the forged documents. It can be found that the document is used by the forger or another individual, not involved in the forgery. The forger then follows to be found.

8. Check if there is another crime committed in relation to or on occasion of the forgery of the document. There may be a framed forgery aiming to delay or prevent the fraud's investigation, corruption, mismanagement or other.

9. Establish the type of forged documents - official or private, primary and secondary accounting documents, registry, etc. To find whether the documents have been partly or entirely falsified one needs to check the whole content.

10. Check if there is a schedule for document flowchart and whether it provides the document type being processed. Controlling the period of moving the document from its creation to finding the forgery.

11. Check the control version of the technical means by which the forgery was found. Measures must be taken for finding the initial text in the original document. In many

cases, these are well planned and prepared criminal acts. Control the presence of arithmetic and technical errors, incorrect determination of aggregate variables and possible inaccuracies in data transmission.

12. Clarify the individuals entitled to issue, use, transfer, archive and destruct forged documents. When storing documents requires specific conditions (such as payroll), the extent of compliance should be determined.

13. Find the caused damage and on whose account the result is. Establish the possible perpetrators of the crime - destruction, damage, concealment, etc. Take comparative material from other documents written by the respective individuals. Identify the specific skills and competencies to perform the act.

14. Identify data supporting further investigation procedures and proof of document forgery. Clarify the technical means of document forgery. The revenue authorities control the terms and conditions that made possible the realization of documentary forgery.

15. Determine whether the person is under the administrative jurisdiction of our state. Enter the data for the person's position - the individual may be an official or may have committed the offense while performing official duty. Check for the presence of documents created by persons without assigned powers and professional competence.

16. Collect two types of data about the person - considering the identification of the perpetrator and the potential responsibility for their actions. Indicate the person's age and the soundness of his/her mind. A mental illness influences the subjective element of the offense - fault. Conclude if the person has accomplices and previous similar offenses.

17. Explore prevention possibilities. These can cover the procedure for document access; representative checks; avoidance of pre-signing a blank sheet of paper or an unfinished document; signing each page of important documents and destruction of blank spaces which can be supplemented with added text; controlled access to technical means for copying documents, etc.

IV. ASPECTS OF TAX-SHELTERING CONTROL IN ACCORDANCE WITH THE DIGITAL ECONOMY AND VIRTUAL ACTIVITIES.

A report of the EU Commission states that "investment in digital economy is the key to Europe's future welfare."¹⁵ Digital economy is based upon the information and communication technologies (ICT). Today "6 out of 10 Europeans use the Internet."¹⁶

¹⁵ European Commission - IP/10/571 17/05/2010

¹⁶ See <http://ec.europa.eu/>, last updated on 15.10.2013



1. Digital economy helps establishing and developing the *online single market*.¹⁷ The strategy "Europe 20-20" aims to roll-out broadband Internet access with a speed of 30 Mbps or more to all Europeans. At this stage member states differ in their degree of development of e-commerce and e-business, and cross-border transactions are limited. Only 54% of Internet users in European countries buy or sell goods online, while 22% of them do so from other EU countries.¹⁸

1.1. Electronic commerce. Business transactions are registered under certain regulations.¹⁹ Compliance with the legal requirements for electronic commerce is controlled. It is possible that the "trader" is an individual who is not registered under the Commerce Act, Cooperatives Act, etc. Anonymity of virtual environment trading is supported by the possibility of anonymity in creating a fictitious addressee. Lack of correct documents increases the so-called "black economy" and nonpayment of taxes.

1.2. Tax and social security liabilities payment can be avoided through **home delivery order sales**. It can be characterized by trades made by a limited number of individuals registered in an in-house system. A problem for the revenue authorities is the possibility to set up temporary documents containing summarized data. It is possible to combine doorstep catalogue trade with website advertising and cashless payment, which is out of the scope of control actions.

1.3. Crowd-funding (краудфандинг - in Russian) is an alternative financing method.²⁰ This involves raising funds from various depositors for an advertisement idea they want to back. A problem for the revenue authorities is the lack of adequate legislation documents. Information on sites advertising funding ideas shows that investors are rarely involved in the distribution of profits from the funding and often receive various small prizes through lottery. Document flowchart reporting the income and expenses of taxable activity is of interest for tax purposes.

1.4. Social relationships for exchange of goods and services while avoiding cash payments and participation in the social security system. Such *quasi-market relations* exist in giving presents; performing activities in exchange for another service or natural product; participation in closed societies, groups, clubs - doctrinal, religious, charitable, etc.; creating time banks to exchange services or support; use of generally available (free) goods - digital books, music, movies, etc. Each of these activities is based on the possibility of tax evasion.

2. Existence of undocumented virtual activities (fully, partially or containing replaced data). In addition to changes in the document's nature and content occur new activities connected with virtual environment documentation. They are subject to fiscal control because of the receiving of taxable income / revenue. In many cases they do not constitute documents verified by the revenue bodies, or the temporarily made forged documents are being destroyed. Activities through which taxation is avoided can be:

2.1. Setting a **virtual office**.²¹ In many cases the virtual office is used for anonymous transactions, including through an intermediary. A similar case is registering a **virtual registry office**. The electronic documents relevant to taxation process and may be forged are subject to tax control.

2.2. Appointment of **virtual house-management, supplier, sales expert**, etc. Each paid activity is a fiscal legal fact and leads to liabilities. This method makes it possible to "go round" tax and insurance, accounting, labor, etc. legislation. Finding of documents about the type of legal relation (employment or obligatory) and the due tax and insurance payment is also subject of tax control. The same applies for holding **virtual training** aiming to facilitate the participants. Currently there are similar courses especially for language learning. The sums are paid cashless, often by mail order, to the teaching person subject to tax control on reporting and taxation.

2.3. **Virtual lobbying and creating goodwill against payment.** *Lobbying* is commonly used in countries with developed democracy to influence decision-making. It is performed legally and is advertised for social and fiscal goals. This model of lobbying is not widespread in our country, which doesn't mean it doesn't exist. Its existence is more common in the black economy. Similarly, there are activities aiming to achieve *good reputation*. The practice is to pay for posting (anonymously) on different sites, e-media, etc. In many cases these activities are subject of the (non-taxable) corrupt deal. Establishing actually received sums or acquired property is also liable to tax control.

2.4. Existence of a **virtual currency** used for valuation of goods and services exchanged. This practice is based on the clearing payment systems by redeeming of claims. It has been modified as an anti-crisis activity and has been implemented in several Argentine cities during the 2001 crisis. Subsequently, in 2009, Greece introduced the so-called "local or social currency" that is informal and used by a limited number of individuals. In Patras was created a company ("Ovolos") with a website of a few thousand registered users exchanging goods and services, which are

¹⁷ http://ec.europa.eu/information_society/newsroom/. Last updated on 09/10/2013

¹⁸ http://europa.eu/rapid/press-release_IP-10-571_bg.htm. Last updated on 09/10/2013

¹⁹ Electronic Commerce Act, updated Darzhaven Vestnik, issue 51 of 23 June 2006, art. 4.

²⁰ See <http://inews.bg/>, last used on October 5, 2013

²¹ See Мавродијева, И. Виртуална реторика: от дневниците до социалните мрежи. УИ „Св. Кл. Охридски“, С., 2010 г., с. 79-204.

valued by the novel virtual currency called "ovolos."²² Later, in Volos was created a similar movement carrying actual exchange of clothing and services paid in virtual currency.²³ In 2012, in Athens exists a site known to its thousands of users as an "e-bank of time."²⁴ Its organizing includes information about the free exchange of services for a fixed time period. Despite the specifics of application in the Greek cities of Patras, Volos and Athens, there is the same mechanism *of undocumented barter and payment in virtual currency*, instead of euro, for daily trading. This method for reducing the crisis' impact in Greece hinders the possibilities for tax control and *leads to avoiding tax-payment*.

Another currently used virtual currency is - *BitCoin*.²⁵ The idea for it was developed in 2008 as a mathematically coded money equivalent by an anonymous Japanese author with the pseudonym Satoshi Nakama. Since the year after until now (2009 - 2013) it's been applied by specialized commercial websites users for making real trading online. BitCoin cannot be forged and is untraceable, which prevents the potential control.²⁶ It serves for *anonymous e-commerce and avoiding tax liability*, associated with forging documents.

The gradual coming of new virtual activities increases the share of digital records. In many cases an array of electronic data is not considered a set of e-documents because it doesn't comply with the statutory requirements of the Law for the Electronic Document and Electronic Signature. It is necessary that the group of real economic (commercial) activities, advertised, negotiated and paid for in virtual environments, have an appropriate *virtual tax (fiscal) control*. Its implementation requires the use of new specific regulations, methodology, technology and organization. *Virtual tax control* should be directed to *the data for taxable transactions and activities contained in the information from the virtual environment, the so-called "Cloud Services"*.

Introducing virtual tax (fiscal) control **needs adequate training of control specialists-to-be**. The rapid technology development gives reason to expect that the existing computer games, including the so-called "virtual worlds" (depicting real life situations), can be adapted for innovative learning. Artificial computer environments can be used for training *through simulation control*. Such training motivates the application of *role-playing games, open and latent control procedures* for identifying forged, hidden, backdated documents or of false nature (by an unauthentic author, identity theft, signature imitation / disguised handwriting, etc.) or containing incorrect information with false documentation.

²² See money.bg and http://news.ibox.bg/news/id_1504117176. Last updated of 09/10/2013

²³ See <http://www.investor.bg/> Last updated on 09/10/2013

²⁴ See http://money.bg/comment/id_1749670346. Last updated on 09/10/2013

²⁵ See <http://news.expert.bg/n421089>, last used on October 5, 2013

²⁶ See <http://www.coindesk.com/information/who-is-satoshi-nakamoto/>. Used on October 5, 2013

V. CONCLUSIONS

To sum up, these aspects of tax-shelters control are a small part of many possible. Globalization processes require complex international measures for control countermeasures. Avoiding tax and social security liabilities is an issue facing supervisory authorities in our country. The report of the National Revenue Agency (NRA) states that "the accumulation of overdue liabilities to the budget since 1991 to the end of 2012 amounts to 18.9 billion leva". This is an increase with over 2 billion leva for one year. According to NRA data, 80% of the debt is bad, and 11.2 billion can be characterized as tax fraud, as they have been found through audit reports under the VAT Act."²⁷ Although legally established, these sums cannot be collected. The reason for that is that debtors are individuals who do not own property towards which to direct coercive measures.

This requires updating the methodology, organization and technology of control on tax-shelters in order to achieve adequate prevention.

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²⁷ See <http://www.pariteni.bg/>, last updated on 15.10.2013