THEORETICAL INSIGHTS AND PRACTICAL CONCERNS ON TAX COMPLIANCE IN POLAND

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Abstract - In the face of the continuous growth of public expenditures there is a pressing need to improve the efficiency of tax collection. This goal may be achieved both by decreasing the costs of tax administration and increasing tax compliance. Before designing a plan for tax compliance maximization and implementing the appropriate measures governments have to research the scale and factors of non-compliance. The problem of tax (non) compliance is addressed in this paper. It first presents the definition and determinants of tax compliance on the basis of economic literature. In the second and third part it concentrates on tax compliance in Poland. The second part includes the aggregated data illustrating the scale of tax evasion. The third – presents the results of tax compliance audits conducted in Poland in the years 2010-2016 and inter alia takes into account such indicators as audit coverage or additional tax liability assessed as a result of tax audits.

Index terms - Tax compliance, Tax evasion, Tax audit.

I. INTRODUCTION

Taxpayer compliance is an important topic of discussion both from the theoretical and practical point of view. The main reason is the relevance of taxes as a source of financing of public expenditures. In the OECD member states taxes and social security contributions constituted in 2015 approximately 34,0% of GDP, while for the European Union member states their share in GDP reached nearly 38,7%. Lack of proper means to safeguard tax compliance may lead to substantial revenue losses and even endanger the financial system of a country. Tax compliance may be approached, analyzed and evaluated from many different perspectives. On the one side enhancing tax compliance is a prerogative for governments that peruse the goal of efficient tax revenue collection. On the other taxpayers that seek to maximize their after-tax-income are making attempts to be non-compliant. The large scale of tax evasion is usually attributed to ineffective tax administration. However the reasons for that phenomenon may be diverse and deliver a basis for many concepts of tax compliance. These concepts derive both from conventional economic theories and behavioural economics. Moreover the origins of some theories that emerge in the process of tax compliance analysis may be found in disciplines, commonly overlapping with economics such, as: sociology, psychology or even neuroscience.

This paper reviews the main factors of tax compliance as analyzed in the economic literature. Moreover it is devoted to the problem of tax non-compliance in Poland. It compares the scale and structure of tax losses due to tax evasion in Poland and other European Union member states. Finally it presents the main result of tax audits conducted by Polish tax authorities in order to ensure tax compliance.

II. DEFINITION AND FACTORS OF TAX COMPLIANCE

Tax compliance is usually researched by taking into account two approaches: the narrow one and the wider (James, Alley 2002, p. 33). The first perceives taxpayers as rational agents who are making decisions aimed at the maximization of their own utility. They are complying with the tax law as long as the benefits from compliance exceed the costs of breaking the law. The second examines a broader scope of factors that may have an effect on taxpayer behaviour and treats the taxpayers as citizens engaged more or less in the process of building common welfare. Considering the first approach tax compliance may be simply defined as the degree to which taxpayers fulfill their tax obligations. Non-compliance may be measured in this approach in the form of a tax gap representing the difference between the actual tax revenue collected and the so called theoretical tax revenue which means the revenue that would be collected if all the taxpayers were fully compliant. Within the second approach compliance is not enforced but voluntary and described as the willingness of citizens to pay their taxes. Non-compliance in that approach covers not only deliberate tax evasion but also tax avoidance.

The narrow approach to tax compliance has its roots in the economic deterrence model developed by M. G. Allingham and A. Sandmo (1972, s. 323). It is based on the assumption that taxpayers are utility maximisers, equipped with the knowledge about fraud detection rates as a result of tax audits conducted and penalties imposed in the case of detection. According to this model tax compliance may be improved by increasing either detection rates or penalties. The failure of increased detection rates and penalties to significantly affect tax compliance in the United States in the 1980s resulted in the formulation of alternative models. These models blend the main assumptions of the deterrence model and certain findings from other scientific disciplines. They take into account such factors of tax compliance as, inter alia: tax design, taxpayers' income, personal and social norms, perception of tax fairness, tax morale, age, sex, political preferences, nationality.

Among the most commonly discussed determinants of tax compliance are tax morale and the perception of tax fairness. Authors provide for diversified definitions of these two determinants. As indicated by E. F. P. Luttmer and M. Singhal tax morale is often defined as an umbrella term including non-pecuniary motivations of tax compliance and factors that fall outside the standard expected utility framework, e.g. intrinsic motivations (feeling of guilt or shame), reciprocal motivations, peer effects and social influences, long run cultural factors (2014, p. 150). Similarly fairness is described broadly. It is often used interchangeably with the notions of equity or justice and covers distributive justice (related to the balance between tax payments and the public goods received in exchange), procedural justice (related to the quality of administrative procedures and treatment in interactions between taxpayers and tax authorities), retributive justice (related to the responsibility for tax non-compliance) (Kirchler, 2009, pp. 75-87).

The review of the papers examining tax morals and perception of tax fairness as factors of tax compliance is included, among others, in the publication by K. Devos (2014, pp. 28-49). The author argues that the majority of the studies indicate the existence of a strong relationship between tax morals and tax compliance which means that taxpayers who posses higher moral values are more likely to be compliant. The literature exploring the significance of tax morale for tax compliance is also analyzed by B. Torgler who emphasizes inter alia the effect exercised by a high level of corruption and the shadow economy on taxpayer decisions (2011, p. 54). In a country where citizens are not protected by the rules of law the incentive to be non-compliant increases significantly. On the other hand a fair and respectful treatment of taxpayers may encourage the taxpayers' readiness to adhere to their tax obligations.

In the case of tax fairness the results of research conducted by different authors are inconsistent. The positive correlation between tax fairness and tax compliance may be explained inter alia by the fiscal exchange theory. It implies that the quality of public goods may affect taxpayers' decisions – the higher the quality, the more compliant are the taxpayers. Arguments supporting this correlation may also be raised on the basis of comparative treatment theory. It is related to the principle of equity in taxation and suggests that taxpayers are more likely to comply with tax regulations if they perceive the system that determines these rules as impartial (Fjeldstad, Schulz-Herzenberg Sjursen, 2012, p. 11).

Certain researchers argue that the relationship between perception of tax fairness and tax compliance may not be straightforward to discover. For instance the study by W. K. Smith examining the association between these variables indicates that taxpayers who evaluate the tax system as fair may be likely to evade taxes. An explanation of this phenomenon was delivered inter alia by A. de Juan et al. They point out that taxpayers who think they are paying less taxes than they should (find themselves in a more advantageous tax situation) have a tendency to be more compliant (Devos, 2014, p. 42).

Tax compliance is also affected by other determinants such as demographic factors. Although scientists are unable to explain the reasons for existing correlations the following facts were discovered as a result of research conducted (Kornhauser, 2007, p. 154):

– in relation to gender as a determining factor most studies suggest that women are more compliant than men, in addition women respond better to positive appeals. On the contrary men were found to respond better to negative and normative appeals;

– in connection with age researchers observed that older individuals have a tendency to be more compliant. This phenomenon may be related to the higher social capital, higher risk aversion or knowledge of tax law;

– with regard to marital status findings are mixed although some studies clearly demonstrate that married people are less compliant than single individuals;

– similarly diversified results concern education. Education may lead to the internationalization of social norms and as a result increase tax compliance. On the other hand educated people may have a greater knowledge of tax law, including knowledge about tax avoidance, tax evasion schemes and their application;

– with reference to income of a taxpayer the results of studies conducted are also contradictory. However some studies show that poor people are more opposed to tax evasion than the wealthy ones;

– with regard to religion the findings are more homogeneous. Being religious is usually positively correlated with tax compliance. As is explained by M. E. Kornhauser this correlation exists because religion acts like a "supernatural police" or because religion is a proxy of such variables as ethics. There are however a few exceptions. Some studies indicate that the correlation may be negative, inter alia B. Torgler examines the effect exercised by the religions on taxpayers' behaviour and discovers a strong correlation between religiosity and tax morale. According to the results of the study however not every religious belief has a positive effect on tax compliance. Being protestant may be related to a relatively strong opposition to taxation (Torgler, 2003, p. 15).

III. SCALE OF TAX EVASION IN POLAND AND SELECTED EUROPEAN UNION MEMBER STATES

Studies devoted to tax compliance in Poland are scarce. Most of the authors analyze the phenomenon of tax evasion while taking into account its scale and structure. Determinants of the scale of tax evasion are considered and researched very rarely. In economic literature tax evasion is perceived as the most relevant symptom of tax non-compliance. Tax evasion differs from the other tax non-compliance behaviours owing to the fact that it is illegal in nature. Taxpayers either do not disclose to the tax authorities the factual or legal state of their financial affairs or provide information that is erroneous (incorrect) on purpose. According to the opinion of M. Bhandari tax evasion involves: non-compliant behaviour of a taxpayer (nonpayment or underpayment of taxes owed), intentional violation of the tax law and taking affirmative steps to avoid detection by tax authorities (2017, s. 63-64). While tax avoidance may be perceived from the point of view of violating the social contract, tax evasion should be treated as a form of crime (Tooma, 2008, s. 14). In principle the term – tax evasion – is employed interchangeably with the term – tax fraud.
The attempts to estimate the scale of tax evasion undertaken by numerous authors and government institutions lead to inconsistent results. That is due to the fact that the phenomenon of tax evasion is difficult to observe and measure. The surveys and experiments are used to analyze this scale relatively frequently. Many studies present the estimates of the so-called tax gap. This gap is defined as the difference between the amount of tax that taxpayers should pay and the amount that is paid voluntarily and on time. The tax gap may be applied as a measure of the scale of tax evasion or tax non-compliance as is defined in its broader sense. It must however be underlined that it is commonly estimated when taking into account the tax losses due to not only tax evasion but also tax avoidance, unintentional mistakes committed by taxpayers while declaring tax due and tax arrears.

According to the estimates by K. Raczkowski the relation of the tax gap to the GDP for the EU-28 reached nearly 10.7% in 2014 (Table. 1). This relation was the highest in such member states of the European Union as Italy, Estonia and Romania and was relatively high for Greece, Hungary, Malta and Spain. It was the lowest in Luxembourg, Ireland, the United Kingdom, Denmark and the Netherlands. Tax gap as % of GDP in Poland did not exceed the EU-28 average. Comparing the tax loss due to tax non-compliance in billions of $ in the EU member states results in a different ranking of countries. The highest loss was observed for Italy, Germany and France, the lowest – for Luxemburg and Malta. Poland in 2014 suffered a tax loss that was approximately at the EU average.

Table 1: Tax gap in Poland and selected EU member states in 2014

EU Member States	Tax gap (% of GDP)	Tax gap (billion $)
Austria	3.9	17.02
Belgium	9.5	50.56
Bulgaria	8.4	4.69
Cyprus	5.8	1.36
Czech Republic	7.5	15.45
Denmark	3.4	11.56
Estonia	13.6	3.52
France	6.6	186.54
Germany	6.3	244.41
Greece	11.8	27.98
Hungary	10.6	14.54
Ireland	3.2	7.77
Italy	13.8	295.90
Luxembourg	1.6	1.01
Malta	10.1	1.01
Netherlands	3.5	30.86
Poland	9.2	50.47
Portugal	8.1	18.50
Romania	12.3	24.41
Spain	10.8	152.02
Sweden	6.9	39.18
United Kingdom	3.3	96.17
Average EU (EU-28)	10.7	51.87

Source: Raczkowski, 2015, s. 67-68.

Substantial tax losses in the European Union member states are caused by VAT fraud, especially the so called missing trader fraud that is a consequence of the application of the destination principle, which provides for taxation in the country where the purchaser of the goods resides. According to this principle taxes are imposed on intra community acquisitions and imports and rebated on intra community supplies and exports. VAT fraud usually takes the form either of an acquisition fraud or carousel fraud. Acquisition fraud results in goods being imported from another country and sold to the local costumers by a trader who goes missing without submitting tax return and paying tax on both transactions. Although carousel fraud resembles acquisition fraud in its first stage it is more sophisticated in its organizational structure. The goods acquired from another country are not sold for consumption on the home-country market of the trader but they are traded through a series of companies and then re-exported to another country (they are moving in a pattern that resembles a carousel).
Research conducted by the European Union indicates the existence of a significant scale of VAT fraud in many member states. Tax losses due to this fraud amounted to EUR 151.5 billion in 2015 (12.8 percent

of theoretical VAT revenue). In the ranking of countries with the highest VAT gap the first places were occupied by Romania, Slovakia and Greece. In Romania the estimated VAT gap equaled 37.18 percent of theoretical revenue (Study to quantify, 2017, p. 17). Poland was ranked 6th with the VAT gap at 24.51 percent of theoretical revenue. Estimations of the VAT gap in Poland were also presented in the report published by Pricewaterhouse Coopers. In the years 2007-2016 VAT gap in relation to GDP increased from 0.6% to 2.5% (Wyłudzenia VAT, 2016).

IV. AUDITING TAX COMPLIANCE IN POLAND

In order to strengthen the powers and redefine the obligations related inter alia to auditing tax compliance the structure of tax administration in Poland underwent a comprehensive reform, with effect from 1 March 2017. Under the current regulations the jurisdiction over the audits of tax compliance is divided between two types of authorities:
– directors (heads) of tax offices who were entitled before the reform and are still entitled to conduct so called tax audits,
– directors (heads) of customs-tax offices who were granted the rights to conduct customs-tax audits after the reform.
The customs-tax audits have a wider scope than the tax audits and may cover the examination of compliance not only with the tax and customs duty law but also, among others, foreign exchange and gambling law. They are also aimed at detection of organized tax crime. The officials conducting those audits are equipped with special privileges which include inter alia the right to undertake operating surveillance activities.
Tax offices conduct field audits in order to examine compliance with tax law. In addition they pursue other activities, including the verification of the documentation submitted by taxpayers in the premises of these offices. Field audits are initiated ex-officio and are aimed mainly at disclosure of economic activities and sources of income not declared for tax purposes, verification of declared tax bases and declared tax due.
The scale of tax (non)compliance may be evaluated by analyzing the results of tax audits, in particular the statistics concerning the number of cases detecting non-compliance and additional tax liability assessed as a result of detection of tax non-compliance. According to the data collected by the Ministry of Finance in Poland tax offices in the years 2010-2016 conducted more than 641 thousand field audits. The number of tax audits decreased systematically year by year (Table 2). The same is true for the audit coverage which declined from nearly 3.5% in 2010 to 1.0% in 2016. There were two main reasons for that decline – the growth in the number of registered taxpayers and improved targeting of tax non-compliance cases. The second factor was in particular due to the increasing application of computer screening as a method of taxpayer selection for examination. One of the tools implemented to select cases for tax audits is the computer software IDEA which identifies potential non-compliance cases on the bases of Bedford law. It is used to discover abnormalities in large data sets and enables the tax authorities to detect falsified data in financial statements. According to this law the first digits in any data are not distributed in a uniform way but follow a logarithmically declining pattern (Tödter, 2009, p. 339).

Table 2: Tax audits conducted in Poland in the years 2010-2016

Year	Number of tax audits	Tax audit coverage (%)
2010	124 854	3.54
2011	131 228	3.58
2012	117 813	3.12
2013	99 630	2.64
2014	79 867	2.08
2015	49 837	1.28
2016	38 421	1.00

Source: Own elaboration based on (MF-9Ps, 2011, s. 1; MF-9Ps, 2012, s. 2; MF-9Ps, 2013, s. 1; MF-9Ps, 2014, s. 1; MF-9Ps, 2015, s. 1; MF-9Ps, 2016, s. 1; MF-9Ps, 2017, s. 2).

In the years 2010-2016 the majority of audited taxpayers were small and medium-sized enterprises submitting personal income tax returns. Only approximately 17.4% were large corporations. Nearly 2,9% of total tax audits were initiated on the basis of external information about conducting business activities not registered with tax authorities.

Table 3: Results of tax audits conducted in Poland in the years 2010-2016

Year	Tax audits detecting non-compliance to tax audits in total (%)	Additional tax liability per tax audit	
		PLN	$
2010	62.37	17 053	4969
2011	68.70	17 764	5176
2012	69.53	22 072	6431
2013	70.46	35 415	10 319
2014	77.03	65 708	19 146
2015	84.23	139 225	40 568
2016	84.42	254 904	74 275

Source: Own elaboration based on (MF-9Ps, 2011, s. 1; MF-9Ps, 2012, s. 2; MF-9Ps, 2013, s. 1; MF-9Ps, 2014, s. 1; MF-9Ps, 2015, s. 1; MF-9Ps, 2016, s. 1; MF-9Ps, 2017, s. 2).
1 Dollar = 3.4319 PLN, 24 March 2018

The ratio of audits detecting non-compliance to total audits conducted by tax offices in Poland recorded an upward trend in the years 2010-2016. It increased from 62.4% to 84.4%. A constant increase could also be observed in the case of additional tax liability per tax audit (Table 3). Both were due to the increasing efficiency of the audits and the rapidly growing scale of tax non-compliance, especially related to VAT underreporting and VAT fraud. The most common VAT non-compliance behaviour in Poland included falsifying refund claims, forging invoices, fictitious transactions (especially intra-Community transactions), disguising domestic sale as international transaction (export, intra-Community supply), missing trader fraud, underreporting sales in order to avoid registration for VAT purposes, purposefully misclassifying commodities in order to increase the proportion of sales subject to lower tax rates.

For that reason in the last six years tax offices concentrated more and more on verifying compliance with VAT obligations. In 2010 nearly 55.9% of the total number of tax audits were aimed at examining VAT taxpayers. This percentage increased systematically and reached 68.6% in 2016. As it is illustrated in Figure 1 more than 92.0% of additional tax liabilities in 2016 were assessed also in relation to VAT.

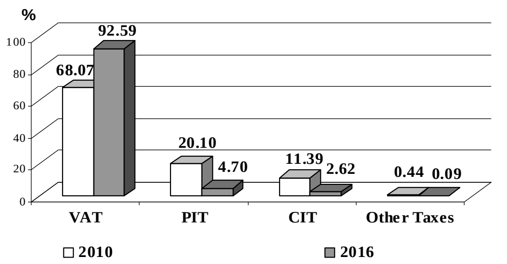

Figure 1: Structure of additional tax liability as a result of audits conducted in Poland in the years 2010-2016 by types of taxes
Source: Own elaboration based on (MF-9Ps, 2011, s. 2, MF-9Ps, 2012, s. 3, MF-9Ps, 2013, s. 2, MF-9Ps, 2014, s. 2, MF-9Ps, 2015, s. 2, MF-9Ps, 2016, s. 2, MF-9Ps, 2017, s. 3).

In order to improve efficiency of tax audits tax offices selected taxpayers for examination on the basis of previously identified risk areas. In 2010 they were related in particular with fraud schemes and covered inter alia VAT underreporting aimed at avoiding registration, intra-community transactions, frequent VAT reimbursement claims. Tax offices also concentrated on auditing selected economic sectors. They included among others: fuel sector, metal recycling sector, trade with mobile phone and electronic devices, trade with imported motor vehicles, provision of intangible services. In 2016 the most likely to be audited were entrepreneurs conducting activities in one or more of the following economic sectors: wholesale trade; counseling, advisory and similar services; financial and insurance services; real estate; construction services and production of construction materials; services of intermediaries and agents; electronics; fuel sector. The efficiency of tax audits, measured both by the ratio of tax audits detecting non compliance to tax audits in total and tax liability assessed as a result of tax audit was the highest for examinations conducted in financial and insurance services and in the case of enterprises providing construction services and producing construction materials.

CONCLUSION

Tax compliance is a complex phenomenon that may be influenced by a wide variety of both economic and non-economic determinants. In the European Union member states taxpayer decisions may be shaped not only by country-related but also international factors. Intra-Community regulations may either positively or negatively affect the scale of such forms of tax non-compliance as tax evasion or tax avoidance. Certain behaviour patterns, in particular fraud schemes, may also be imported from other countries.

This fact is true especially in the case of VAT. Non-compliance schemes are similar in all the European Union member states in regard to this tax due to the harmonization of the tax base and application of common taxation principles. VAT is also perceived as one of the taxes the most vulnerable to fraud. In the European Union member states VAT fraud causes immense losses of tax revenue which in Poland reached nearly 2.5% of GDP in 2016.

Classical theories place much emphasis on enforcement measures as instruments used to enhance tax compliance. That is why they are inevitable components of every tax system. Particular attention in this regard is paid to tax audits which are applied both to detect and to prevent tax non-compliance. In Poland tax audits are considered as a relatively effective method to reduce the scale of tax evasion. The number of audits detecting tax non-compliance and additional tax liability per tax audit are increasing year by year. The main reason for this increase is not only the growing scale of tax fraud but also improved methods of taxpayer selection for tax audits.

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