

# THE TAXES' IMPACT ON THE ENTREPRENEURIAL ACTIVITY DEVELOPMENT

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## **Abstract:**

*The role of taxes is indispensable for the all countries' economy development, taxes having multiple positive and negative effects on micro and macro economic indicators. The level of countries' economic development depends a lot of the business environment development, and, in the end, depends a lot of the different taxes level. The purpose of this article is to conduct extensive research based on the comparative analysis of the taxes level specific of entrepreneurial activity, applied in the Republic of Moldova and the similar experience in different countries of the world. For further research, there is planned the application of the correlational analysis by determining the mathematical model that expresses the influence of the taxes level on the level of the state's development, being argued proposals to improve the situation.*

**Keywords:** *Taxes, entrepreneurial activity, development.*

**JEL classification:** *H2, H21, H25*

## **Introduction**

The economic development of any country depends indispensable on the business environment and the level of development of entrepreneurship in those countries. In this context, more and more attention is being paid to business development, especially in the field of small business. If things are better in developed countries, such as most European Union member states, in developing countries are being implemented various programs to stimulate the development of entrepreneurship. An important role in supporting the development of the business environment is given to the research of the main problems faced by existing entrepreneurs and the problems that prevent the launch of business among potential entrepreneurs.

If we address the issue of taxes globally, there is a high level of variation in taxes, from zero to the highest levels. In this context, it is of particular interest to establish the link between the level of development of the country and the level of taxes and fees related to the business environment applied in these countries. At the same time, some taxes, such as, for example, the level of social insurance contributions vary essentially from one country to another as a level and as a distribution of the share established for the employer and for the employee. In this context, some countries impose the burden of the social insurance contributions mainly on the employer, which often stimulates the development of the shadow economy and „wages in the envelope”. On the other hand, there are countries that attribute the social insurance contributions in full or largely to the employee, so that the real purchasing power of the salary is diminished considerably.

In this research, special attention is put to studying the approaches of different scientists and specialists in the field, in terms of the optimal level of taxes and fees to ensure the most favorable level of economic development of entrepreneurship and economic development of the country.

As research methods, there are applied statistical methods of descriptive analysis with an emphasis on the application of variation indicators and on the study of deviations from the standard normal distribution. At the same time, there are applied statistical methods of inductive research, which involve a selective research by sampling.

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In the context of the ideas presented above, this article is oriented towards the comparative analysis of the taxes' level and towards the research of the main related issues. Based on the obtained results, there are formulated scientifically substantiated measures in order to establish the optimal level of taxes that will be able to stimulate the entrepreneurship development, ensure a competitive level of income for the population and ensure the necessary level of revenue in the state budget.

## Description of the Problem

One of the main problems that is quite frequently raised by entrepreneurs operating in developing countries, especially in cross-border areas, is the issue of high levels of taxes. In the Republic of Moldova, a good part of the entrepreneurs attest that a correct activity by respecting and paying in full the related taxes and fees makes their activity unprofitable, so some entrepreneurs prefer to avoid paying some taxes.

Studies conducted among young people also show a highlight of the problem of high taxes, which prevent the launch of new businesses. In order to improve the youth entrepreneurship environment in the framework of the HEIFYE project in the Republic of Moldova, 422 youth respondents filled out a youth entrepreneurship survey. One of the survey directions was to evaluate the above factors in terms of their importance in order to encourage young people to start a business or help develop an existing business (Turcan Iu. & Turcan R., 2020, p.108).

**Table 1**

### Evaluation of financial factors in terms of the impact on youth entrepreneurship in the Republic of Moldova

Nr.	Factors	Points
1.	Accessibility of financing in general for starting a business	3,44
2.	Accessibility of financing of European and other funds	3,31
3.	Investor Finance (Business Angels)	3,22
4.	Personal savings	3,21
5.	Accessibility of state and regional funding programs	3,21
6.	Tax rebates	3,16
7.	Bank financing	3,05
8.	Attraction and use of collective financing	2,96
9.	Financial assistance from friends and family	2,89
10.	Financing Venture Funds	2,68

Source: Presentation of research results "Youth Survey" - Higher educational institutions for youth entrepreneurship, HEIFYE Project, Co-funded by the Erasmus+ Programme of the European Union, 2018, <http://heifye.hduht.edu.ua/index.php/en>

The survey's results show that young entrepreneurs consider that the impact of taxes is considerable on the development of entrepreneurship, it is rated 3.16 points and occupies the sixth position in the rating financial factors in terms of impact on youth entrepreneurship in the Republic of Moldova.

In the context of the above, there is raised the issue of comparative research on the level of taxes and contributions applied in various countries of the world, with priority given to the situation in the Republic of Moldova and in the European Union countries. Thus, there are researched the justifying arguments that will confirm how strongly the level of taxes influences the level of economic development of the country and the main factors that support the development of entrepreneurship even in the conditions of high taxes and fees.

## Methodology and Results

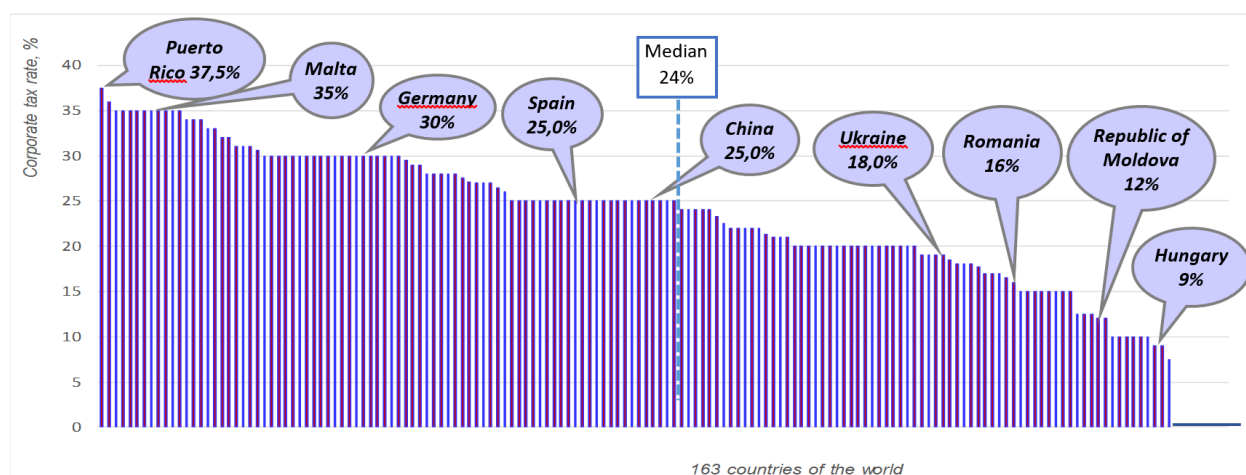
The multiple approaches of the tax systems specific to different countries of the world, finally lead us to the same conclusion, as they aim to ensure an optimal level of taxes, as well as the related principles, so that they correspond exactly to the basis strategies of the state's development.

The effectiveness of fiscal policy is manifested by its consequences on economic activity, because through taxes, both direct and indirect, it intervenes in the process of obtaining and distributing income of economic agents and, respectively, on their financial results (Cuslii Eu., Munteanu T., 2015, p.108).

Income tax refers to direct taxes, since its amount is directly proportional to the taxpayer's final financial result of the economic activity and reflects his actual solvency (Minaeva E., Anoshina Iu., 2019, p.123).

Depending on the level of the country's economic development, as well as depending on its priority objectives, the fiscal mechanism differs considerably from one country to another.

Figure 2 shows the distribution of the world's countries according to the level of corporate tax rate among the 163 countries of the world. Based on the objectives of the research that provides for the argumentation of the level of the corporate tax in terms of the impact on the business environment development, the experience of other countries in this field will be taken into account.



**Figure 1 – Distribution of the world's countries according to the corporate tax rate specific to 2019\***

Source: data collected from <https://tradingeconomics.com/country-list/social-security-rate>. \* on the base of data for 163 countries

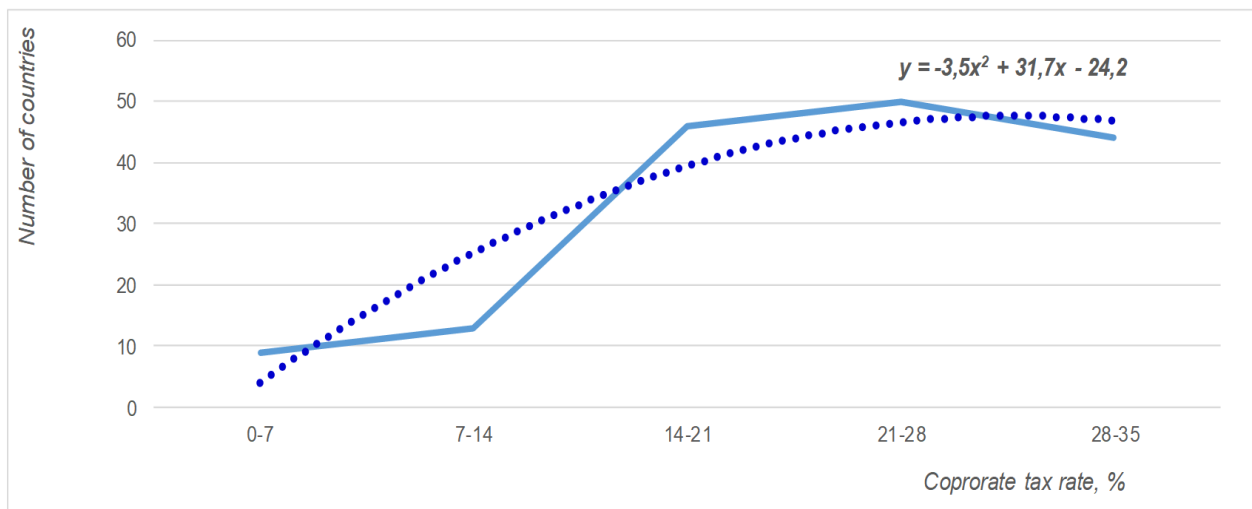
The spectrum of variation of the corporate tax rate is very high, starting with the maximum level of this indicator of 37.5% applied in Puerto Rico and up to the zero level of this indicator applied in the 7 countries of the world, such as: Vanuatu, United Arab Emirates, Isle of Man, Cayman Islands, Bermuda, Bahrein, Bahamas, this zero share of the corporate tax rate is tax haven specific.

Figure 1 shows very clearly that the average level of corporate tax rate for the 163 countries in the world participating in the study, is about 24%. Based on the value of the median, it can be stated that half of the countries have a corporate tax rate higher than 24%, and the other countries - below the level of 25%. In most European countries the corporate tax rate is quite high, the leader in this respect being Malta at 35%, followed by Germany at 30%, Belgium and France at 29%.

The European Union countries that gear towards attracting investment and developing the business environment, there is applied a lower corporate tax rate compared to the average level. In this context, such countries can be mentioned, such as Romania - 16%, Bulgaria - 10%, Hungary - 9%. Another European country in the process of joining the European Union, Montenegro applies a corporate tax rate of 9% to be more attractive to potential investors. Countries located in the cross-border area, such as the Republic of Moldova and Ukraine, have a considerably below average corporate tax rate, which aims mainly to attract foreign investment and business development.

Although potential young entrepreneurs are quite pronounced on the high level of taxes applied in the Republic of Moldova, considering it a negative factor hindering the development of the business environment in the Republic of Moldova, effective entrepreneurs who already know the key issues of business does not consider the level of the corporate tax to be high. In this way, entrepreneurs highlight several other issues in the tax field, such as: the presence in the state budget plan of the item of income from fines and penalties applied to businesses; the inconsistency between the fiscal rules and their imperfection; not using, ignoring or using formal procedures for the preliminary settlement of tax disputes; failure to protect taxpayers in court; lack of liability before the law of persons exercising poor tax administration (Grinic T., 2017, p.4).

The corporate tax is the main tax that is imposed on all economic agents engaged in entrepreneurship has a high level of variation, the distribution being asymmetric on the right, which allows us to conclude that most countries apply the higher level of this tax.



**Figure 2 – Equation of distribution of the world’s countries according to the corporate tax rate specific to 2019\***

Source: data collected from <https://tradingeconomics.com/country-list/social-security-rate>

\* on the base of data for 163 countries

The corporate tax rate distribution differs considerably from the normal distribution curve being deviated considerably to the right. Half of the 163 countries of the world have the corporate tax higher than 24%, in this category being attributed both the countries with a high level of development, as well as the very poorly developed countries. Tax planning can be unfair as it effectively shifts the tax burden on other taxpayers, such as consumers or small and medium-size enterprises (SMEs) which operate at local level (Álvarez-Martinez M and others, 2016, p.6). The strategic goal of business is to optimize the tax base and business with value added and tax reduction in all areas of taxes (Teplicka K., 2018).

With all the above, in the Republic of Moldova the corporate tax rate is quite low, and the reduction of the tax burden in favor of increasing the volume of industrial production can be considered as a successful compromise between fiscal and incentive function, especially in developing countries.

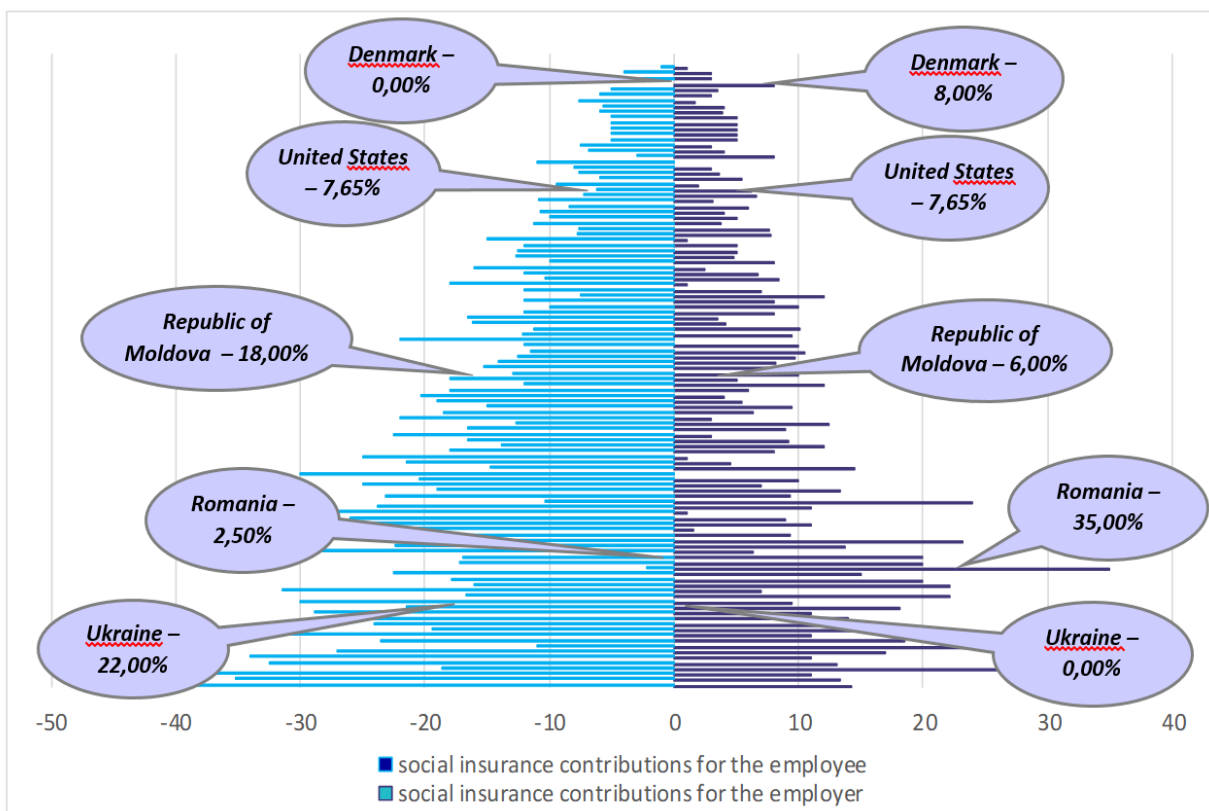
In order to ensure economic growth in the country and at the same time ensure the necessary income in the state budget, reducing the level of corporate taxation is not a strictly necessary measure. Because there are a multitude of other solutions. How, for example, the US has decreased tax rates over time while keeping the income tax revenue as a share of GDP stable (Gillman M., 2020).

Another quite pronounced problem in developing countries is the problem of unofficial wage payments, called the "envelope wage problem". By using the informal payment of the salary or part of the salary, the employer tries to reduce the expenses related to the breakdowns with the state budget regarding social insurance contributions and health insurance contributions. In this context, the employer's payments related to social security contributions differ considerably from one

country to another depending on the insurance system, so that in some countries employers do not participate at all with health insurance contributions for their employees, in other countries dominate private health insurance systems, etc. Thus, an important category of payments for the employer that causes him to resort to informal payment of wages is social security contributions.

Broadly speaking, through the public social insurance system, any state guarantees its citizens the right to social protection in various cases such as: illness, disability, old age, unemployment by providing the beneficiary with social payments in the form of pensions, benefits, etc. In the broadest sense of the word, the social security system, being a component of the financial system, represents a multitude of relationships through which the redistribution of national income is achieved to reduce the impact of social risks.

In countries where the social system is very poorly developed, the level of insurance of the population in need of social assistance is inadequate, which in turn leads to a reduction of the population living standard and a decrease in the population's happiness score. As a result, there are multiple problems related to the intense migration of the population to those countries, in which social policy ensures a high level of the population social protection, ensuring a considerably higher standard of living.



**Figure 3 – Distribution of the world’s countries according to the level of social insurance contributions for the employer and for the employee specific to 2019\***

Source: data collected from <https://tradingeconomics.com/country-list/social-security-rate>

\* on the base of data for 141 countries

The level of social insurance contributions differs considerably from one country to another. In the social year, 2020 Among the European countries that allocate over 25% of GDP for social spending can be mentioned: France, Belgium, England, Denmark, Italy, Austria, Sweden, Germany. The social policy of these countries is well developed and the budget allows for such large-scale social spending. Obviously, for the state, the main source of income that will later be directed to cover various social expenses are social insurance contributions paid by the employer and by the employee.

Insurance contributions vary much more pronounced than the corporate tax that was examined above. Thus, the level of social insurance contributions varies from 0% in Qatar to 68% in France.

Most European countries are in the top countries according to the social insurance contributions. In addition to European countries that promote a strong social policy, a fairly high level of this indicator is also recorded in China at 48%.

In most countries of the world, social security contributions are paid by two parties: the employer and the employee. In the public social insurance system of the Republic of Moldova are established two types of mandatory contributions: the contribution, due by employers and the individual contribution, due personally by some payers, individuals.

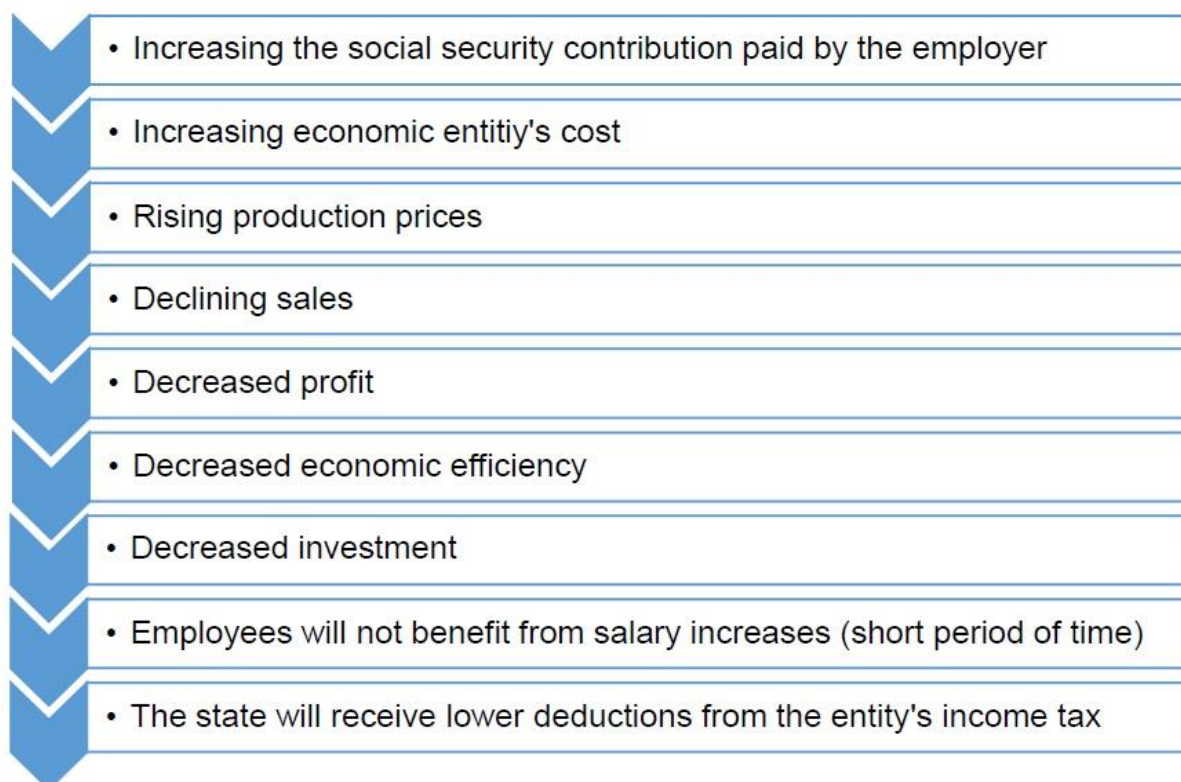
Of great importance is the division of social insurance contributions between employer and employee and these proportions are very varied and differ from one country to another. Figure 3 reflects the distribution of the world's countries according to the level of social insurance contributions for the employer and the employee. The figure presented very clearly shows the distribution of social insurance contributions between the employer and the employee. From the zero axes, the figure has a pronounced deviation on the left side, which allows us to conclude that worldwide social security contributions are covered mainly by the employer, approximately in proportions of 65:35. At the same time, the fiscal policy of some countries differs considerably from the average situation in the world, the most special situations being registered in the distribution of social insurance contributions between the employer and the employee in the following countries.

- Denmark - the employer does not pay social security contributions and the employee pays only 8%;
- United States - the employer and the employee share equally the burden of social security contributions, both paying 7.65% each;
- Romania - the employer pays only 2.50% of the value of social insurance contributions, and the employee bears an imposing share of 35%;
- Ukraine - the entire burden of paying social security contributions is paid entirely by the employer who pays a share of 22.0%, while the employee from his income does not contribute to these breakdowns.

A large part of the countries to which the Republic of Moldova also refers (the contributions of the employer of 18% and the employee of 6%) respect exactly the average distribution worldwide. Considering that in the Republic of Moldova the issue of „wages in the envelope” is a current one, to bring money from the dark economy to the real economy the income tax rate for individuals has been reduced to a single rate of 12%, but it is quite difficult to say that the expected result is obtained. The increase in the level of social insurance contributions for the employee will stimulate a reverse reaction, orienting a part of the population to continue opting for unofficial salaries. The increase in the level of social insurance contributions for the employee leads to a decrease in the purchasing power of the population, which in turn will lead to a decrease in aggregate demand, reducing the effect and efficiency of economic entities. The social insurance system is not only an element of social protection of the population but also a comprehensive financial system. The social insurance system directly influences all participants: the economic entity, employees, and the state. The share of social security contributions represents a part of the company's expenses so that its change will lead not only to the change of the amount paid by the company but also to the change of various economic indicators that characterize the company's activity.

Tax policy has a double dimension in the national economy: one refers to the formation of public financial resources; the second is interventionist, which refers to concrete objectives of involvement, support and encouragement (Timus A., Cociug V., Alfeni L., 2017, p.94).

The increase of the level of social insurance contributions for the employer will have a rather considerable impact, in figure 4 is presented the chain effect of the increase of the share of social insurance contributions for the employer.



**Figure 4 –The chain effect of increasing the share of social insurance contributions for the employer**

*Source: elaborated by author*

Theoretically, it would seem that increasing the level of social security contributions paid by economic entities would lead to increased accumulations in the fund, de facto there are a number of negative consequences, which ultimately lead to more damage to the state budget, than benefits.

One thing can be firmly concluded: in developed countries, although the level of corporate tax and the level of social insurance contributions is considerably higher compared to the average annual value of this indicator, economic agents do not oppose these taxes, respecting precisely the laws. In developing countries, which also refers to countries in the cross-border area, the level of corporate tax and the level of social insurance contributions is considerably lower, which should make economic agents responsible for paying these taxes without dodging. As a result, the state budget has a chronic deficit, which is influenced by both low taxes and the irresponsibility of taxpayers, several other priority factors hinder the development of the business environment, attracting investment, job creation, etc.

## **Conclusions and Future Directions**

The fiscal policy's effectiveness in determining the level of taxes can be assessed by the consequences on economic activities. Although inductive research shows that even in countries with a considerably lower level of corporate tax and social insurance contributions, some entrepreneurs raise the issue of high taxes, the de facto business environment faces a much higher number of problems. In the case of developing countries, a vicious circle is obtained, all problems being interdependent and the low level of taxes is not the cause, but an effect of insolvency.

The social insurance system is not only an element of social protection of the population but also a comprehensive financial system. The social insurance system directly influences all participants: the economic entity, employees, and the state. Based on the collection of the 163 countries around

the world analysed in this paper, social security contributions are mainly covered by the employer, although in some countries there are considerable deviations from this distribution.

For further research, there is proposed the application of the correlational analysis by determining the mathematical model that expresses the influence of the tax level on the level of the state's development, being argued proposals to improve the situation.

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