

Why corruption negatively affects the intention to pay taxes?

Analytical Commentary

Author: Fala Alexandru

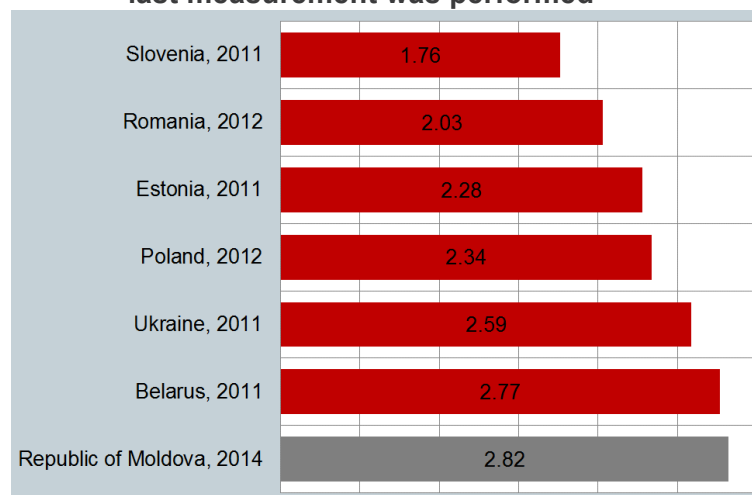
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How Is the Citizens' Intention to Pay Taxes Measured?

Tax morality reflects people's propensity to pay taxes and strengthening tax morality can lead to diminishing the shadow economy. Tax morality is "the moral obligation to pay taxes" and represents „people's conviction that they contribute to the development of the society by paying taxes”¹. In fact, a higher level of tax morality contributes to diminishing the shadow economy². A number of researchers have empirically demonstrated the negative correlation between the tax morality and non-observed economy³. It is also presumed that the use of non-coercive measures aimed at enhancing tax morality would have significant effects on increasing tax compliance⁴.

The level of tax morality in the Republic of Moldova is one of the lowest in the region. According to 2014 estimates, tax morality average score was 2.82 points (see Figure 1). This comparison denotes an unfavourable situation, as the population of the Republic of Moldova has a relatively weak motivation to pay taxes compared to other countries from the region.

Figure 1. The level of tax morality and the year when the last measurement was performed



Source: <http://www.worldvaluessurvey.org>, EG calculations

¹ Recep Tekeli, The Determinants of Tax Morale: the Effects of Cultural Differences and Politics, Policy Research Institute, Japan, in 2011, p.2.

² Ibidem, p. 22.

³ Torgler Benno, Tax Morale and Compliance. Review of Evidence and Case Studies for Europe, World Bank, 2011, p. 11.

⁴ D. Budianschi, A. Lupusor, A. Fala, I. Morcotilo, Independent Think-Tank 'Expert Group', Chisinau, 2014, p. 23.

How Does Corruption Affect Citizens' Intention to Pay Taxes?

Corruption influences tax morality and affects citizens' attitude towards paying taxes.

Countries with high levels of corruption lack the social norm of paying taxes to the Government⁵. Likewise, corruption directly contributes to reducing tax morality and indirectly diminishes confidence in the tax administration system⁶. At the same time, the relationship between corruption and tax morality is much more complex – the two phenomena coexist and reinforce each other⁷.

Manifestations of corruption in the Republic of Moldova, such as accepting bribes or undeserved privileges from the state, also diminish the level of tax morality. The application of quantitative methods⁸ allowed identifying the following variables which have an impact on tax morality: justification of undeserved privileges from the state⁹, justification of accepting bribes, justification of the unofficial salary and informing the population about the use of public money (see Annex 1). Obtaining state privileges and bribe-taking are manifestations of corruption, and receiving unofficial salaries has direct implications on corruption.

Justification of unofficial salaries has the greatest influence on morality, while the changing attitude towards getting bribes, as well as the changing opinion about claiming unjust state privileges, have a lower impact. Changing the attitude towards receiving unofficial remuneration from a negative to a positive one will increase the probability of consolidating tax morality by 7.59% (see Figure 2). Informing about the use of public sources is the second factor to impact tax morality: increasing budgetary transparency will increase the probability of improving attitude towards paying taxes by 5.42%. Changing the opinion on accepting bribery and claiming unjust benefits from the state have lower impact on tax morality: 4.83% and 4.53%, respectively. The negative relationship between corruption manifestations and tax morality can be explained by the fact that, in order to avoid penalties that could be imposed by the state, it is unlikely that persons obtaining unofficial payments declare the true value of their incomes or assets. Citizens are also more willing to pay taxes when they are not deceived by the state and know exactly how public money is used. In countries where corruption is systemic and the government budget lacks transparency it cannot be assumed that the obligation of paying taxes is an accepted social norm¹⁰, because the people have less incentives to pay taxes.

⁵ Torgler (2006) taken from J. Björn, How does petty corruption affect tax morale in sub-Saharan Africa?, United Nations University World Institute for Development Economics Research, 2017, p. 2.

⁶ J. Björn, How does petty corruption affect tax morale in sub-Saharan Africa?, United Nations University World Institute for Development Economics Research, 2017, p. 12.

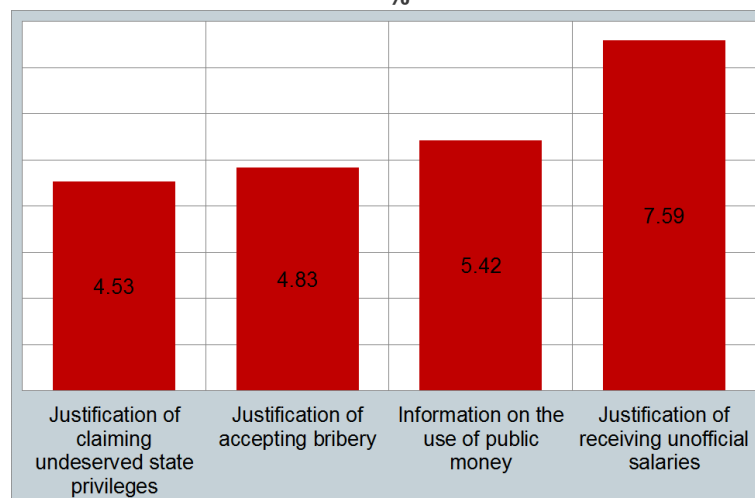
⁷ Amundsen (1999) and Barreto and Alm (2003) taken from A. Litina, T. Palivos, Corruption and tax evasion: reflections on Greek tragedy, Bank of Greece, 2015, p. 3.

⁸ To establish the determinants influencing tax morality, the model ORDERED PROBIT was used. The ORDERED PROBIT model is used when the dependent variable has values that represent a fixed number of options. In our case, the dependent variable reflects the level of tax morality and can have values between 1 and 10: where 1 corresponds to the option 'it is not justified to state a lower income just to pay less taxes' and 10 is associated with the answer justifying non-payment of taxes.

⁹ 'Obtaining undeserved state privileges' reflects the situation when a person in the public service makes use of the duties assigned to obtain personal privileges.

¹⁰ B. Torgler, Tax morale, trust and corruption: Empirical evidence from transition countries. Working Paper No 2004 – 05, Center for Research in Economics, Management and the Arts, p. 10.

Figure 2. Reaction of tax morality to changing determinants,
%



Source: EG calculations

Due to endemic corruption, we can speak of a society ‘infection’ manifested by increased tolerance toward this flaw. If taxpayers might get the feeling that their intrinsic motivation is not recognized or honored if they notice that many public officials are corrupt and many others evade taxes¹¹. As a result, citizens can adopt an opportunistic behavior to make use of unofficial payments and non-payment of taxes. In this context, it should be noted that there is a direct relationship between the attitude towards corruption and the spread of corruption. In fact, it was proved that people in high-corruption states have greater tolerance to this phenomenon¹².

The scale of unofficial activities and schemes is also determined by the poor economic development of the Republic of Moldova. The application of the PROBIT model revealed a significant statistical relationship between income levels and attitudes towards unofficial payments and activities (see Annex 2). People who tolerate bribery acceptance, under-the-table wages or undeserved privileges from the state have a higher level of income than those who do not tolerate such practices. This finding proves that citizens either benefited from or would not refuse the benefits derived from improper behavior: receiving unofficial payments or privileges or obtaining a benefit by bribing an official who accepts bribery. In fact, statistical correlations reveal a sad reality: the economic system is underdeveloped and offers few opportunities, while the role of shadowy activities increases as they can provide additional income for the people.

What Needs to Be Done?

The relationship between tax morality and corruption must also be seen in the context of the poor performance of the economy. The lack of economic opportunities “pushes” Moldovans into unofficial activities, which can provide them with extra income. As a result, citizens become more tolerant to illicit practices, which affects tax morality. Gathering unofficial revenues deters citizens from declaring the real value of their earnings and, implicitly, from paying the corresponding taxes. Citizens also compare the benefits of obtaining unofficial

¹¹ B. Torgler, Tax morale, trust and corruption: Empirical evidence from transition countries. Working Paper No 2004 – 05, Center for Research in Economics, Management and Arts, p. 18.

¹² Cameron, Chaudhuri, Erkal and Gangadharan (2009) taken from J. Björn, How does petty corruption affect tax morale in Sub-Saharan Africa ?, United Nations University World Institute for Development Economics Research, 2017, p. 3.

payments with the advantages of honest behavior and payment of taxes. Given that the payment of taxes translates into bad quality public services, the citizens' propensity to pay taxes declines. At the same time, corruption affects citizens' confidence in the state, harming the intention to pay taxes.

The key ingredient that would enhance tax morality is boosting the country's socio-economic development process – a condition that would increase opportunities for citizens and diminish the role of unofficial activities. In this regard, besides the reforms aimed at improving the economic climate, the changes ensuring the proper functioning of the state are also vital: combating corruption, reforming justice, strengthening public institutions. At the same time, a more efficient public sector would provide quality services and the citizens would feel the benefits of paying taxes and thus reduce the propensity to obtain unofficial revenues.

Informing the people about the budget situation could significantly strengthen the tax morality. Making the budget process transparent would strengthen public confidence in state institutions, which would further foster fiscal compliance. To this end, the authorities should make public institutions more open and pay more attention to communicating with the people.

ANNEX 1

Determinants of tax morality and associated marginal effects, estimation output of the ORDER PROBIT model

Independent variables	Coefficients	Marginal effects
Information on the use of public money	0.136501**	-0.05422**
Justification of claiming undeserved state privileges	0.113974*	-0.04527*
Justification of accepting bribery	0.121661*	-0.04832*
Justification of receiving unofficial salaries	0.191108*	-0.07591*
Number of observations	943	
Pseudo R^2	0.1649	

Source: EG calculations

Note: * – the variable is significant for a confidence level of 1%

** – the variable is significant for a confidence level of 5%

ANNEX 2

Determinants of peoples' income and associated marginal effects, estimation output of the ORDER PROBIT model

Independent variables	Coefficients	Marginal effects
Justification of claiming undeserved state privileges	0.054616*	-0.01213*
Justification of accepting bribery	0.035001***	-0.00777***
Justification of receiving unofficial salaries	0.036698**	-0.00815**
Number of observations	987	
Pseudo R^2	0.0146	

Source: EG calculations

Note: * – the variable is significant for a confidence level of 1%

** - the variable is significant for a confidence level of 5%;

*** - the variable is significant for a confidence level of 10%