TAX MORALE AND COMPLIANCE IN GREECE: A REVIEW OF EMPIRICAL EVIDENCE [(a)]

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ABSTRACT[1]

The main difficulty in the investigation of the level of tax compliance is the lack of detailed and reliable information regarding the behaviour of taxpayers. The paper reviews the main methodologies used by empirical research in assessing the levels of tax morale and compliance, such as laboratory experiments, surveys and field reviews; in turn, it summarizes the empirical evidence from research that has been contacted in Greece and internationally. The paper concludes that there is a significant gap of comprehensive empirical research in the case of Greece. Further, preliminary results from our questionnaire survey are presented.

KEYWORDS
Tax compliance; tax morale; empirical evidence; literature review; shadow economy; questionnaire survey; Greece

JEL CLASSIFICATION CODE
O17 - Formal and Informal Sectors; Shadow Economy; Institutional Arrangements

1. INTRODUCTION

Various studies have been conducted in the past to determine if ethical values, cultural characteristics and habits differ between residents of different countries as well as whether these differences can be measured and affect the economic behavior of citizens. One such field of research consists that of *tax compliance* and *tax ethics*. These concepts while are studied by the economic science, can not be explained and fully understood in purely economic terms. This means that people - taxpayers can not act as purely economic entities whose sole objective is that of maximizing profit or utility. Understanding the problem of tax compliance or tax evasion is a much more complex process and requires the assistance of other sciences, such as sociology, social psychology and political science. Furthermore, it requires explicit knowledge of the workings of the political and social system as well as the functioning of the administrative mechanism of the country under research.

One of the questions that should be answered is who and under what conditions evade taxes and conversely who and under what circumstances comply with their tax obligations. Also a second important question we have to answer is why there are significant deviations in tax behaviors among different states even in cases where a similar fiscal policy is applied. The answers to the above questions will facilitate us to identify and address the root causes of tax evasion.

In an effort to resolve the problem of tax evasion there is a key concept which has spurred far enough research interest of the scientific community, at least at the national level. This is the concept of tax ethics.

2. WORKING CONCEPTS

In the following paragraphs we will attempt a brief analysis of key concepts that will be discussed throughout the course of our research, starting with tax evasion.

According to Tatsos (2001) *tax evasion* means any unlawful act or omission of the taxpayer, which aims at reducing the statutory tax liability and avoid paying the tax. At roughly the same context Alm (1999) states that tax evasion includes all illegal and deliberate actions designed to reduce the tax liability.

A related but not identical concept is that of *tax avoidance* which also aims to reduce the taxable income from the taxpayer's side but using legal means. Particularly, through tax avoidance it is attempted to avoid partial or total tax payment. But while in the case of the tax evasion are circumvented both the letter and spirit of the law, in the case of tax avoidance is circumvented only the spirit of the law, according to Tatsos (2001) and Drakos (1986). In the latter case, the taxpayer tries to exploit loopholes or ambiguities or weaknesses in wording of the Act with a view to reducing its tax burden. The two concepts of tax evasion and tax avoidance are not always discernible. In some jurisdictions they may also be identical. Drakos (1986) uses the general term of *tax-escape* («φοροφυγή») to describe the broader effort of taxpayers seeking to reduce their tax liability and includes activities related to both tax evasion and tax avoidance.

Ethics is a set of values and principles that exist within the consciousness of a person and influence every act of his life. They act independently of any legal rule or any state-imposed compulsion. Such a value or rule may be that of tax compliance. When a person has developed an internal sense of duty to fulfill his tax obligations disengaged from any fear of administrative or criminal sanctions, then it can be argued that a high sense of moral tax has been developed, and that the tax liability has advanced to an internal or ethical rule independent of any exogenously imposed legal rule. According to the above, *tax ethics* is an internal rule or moral obligation to pay taxes (Torgler & Schneider, 2006). It might also be defined as a *conviction* or *belief* based on which it is assessed the act of non-tax compliance in his consciousness. The more contemptible and reprehensible is the act of tax evasion in the consciousness of the person, the higher is the extent of tax morale.

The two concepts (tax evasion and tax ethics) are so closely related that there is a strong negative correlation between them which has also been scientifically documented (Frey and Feld 2002, Torgler 2003, Torgler 2004). The terms tax ethics and tax consciousness will be considered in the present work as synonymous and used interchangeably to avoid repetition.

Finally, considering the *taxpayer's typology*, we might discriminate among four different kinds of taxpayers' behaviors, as previously discussed by Torgler (2003). These types refer to:

1. "Social Taxpayers", which are influenced by social norms and are very responsive especially to the beliefs of the people by which are closely surrounded. They feel culpable when they do not fully report their tax obligations and escape detection and feel embarrassed when they under-report and discovered. They tend to react emotionally to perceived changes next to them. They can be considered as *conditional cooperators*. They depend their actions on their perception regarding others' responses or willingness to respond to their tax obligations. Furthermore, they put a lot of emphasis in the meaning of equity or inequity, justice or injustice. In such cases, it is highly probable, that may engage in behaviors such as tax evasion, aimed to restore equity (Webley et al., 1991).

2. "Intrinsic Taxpayers", which are motivated among others by the feeling of obligation, instead of being acting under the exercise of some external pressure. They are responsive to institutional factors, as e.g., the actions of the government or the way they are treated by the tax administration. Their willingness to co-operate is not conditional to the others' contribution, but they are affected by the institutional conditions prevailing when they must perform their tax payments.

3. "Honest Taxpayers", who do not even consider for means to deceive at taxes. Their attitude does not counter changes in the tax policy parameters, as tax levels, fine rates, or audit frequency. Thus, "their behavior is not subject to a marginal but rather an absolute evaluation" (Frey, 1997). According to experiments, a certain number of taxpayers are inclined to behave frankly irrespective of other conditions.

4. "Tax Evaders", who are characterized generally by a low tax morale and tend to depend their actions on factors such as those considered by the classical economic rational choice theory and particularly the audit probability, or the level of penalty or punishment in case they are discovered. They attempt to maximize their utility by comparing the expected value of evading taxes with the value of behaving frankly.

3. EMPIRICAL RESEARCH

The main difficulty in the investigation of the level of tax compliance is the lack of detailed and reliable information regarding the behavior of taxpayers. The punishability and usually reprehensibility of non-tax compliance consist of the main obstacles in the attempt of any quantitative and qualitative assessments as offenders have an interest in concealing their actions to avoid to be discovered by the authorities. For this reason, the methods most commonly used to accumulate quantitative and qualitative data are the *laboratory experiments* and *questionnaire surveys*. Conducting empirical studies is aimed at testing the extent of reliability of theoretical models. If empirical data coincide with those proposed by the theory then the theory is verified. To a much less extent and *field experiments* have also been used by the scientific community.

The *laboratory experiment* is used in a large scale by the economic science during the last 30 years. A not insignificant number of experiments have been conducted to estimate the extent of tax compliance and the degree of responsiveness or reaction in key economic variables. A significant number of experiments have been performed to examine other, non-economic factors affecting the final decision of the person whether and at what extent is tax-evading. The usual (and justified) criticism of this method is that the laboratory experiments of this type consist of a very technical approach to the outside world and therefore can be considered as unrealistic. In our opinion, laboratory experiments may additionally be used and in parallel with the method of questionnaire. If no major differences are revealed in the application of one or the other method then we might conclude that the estimates of the phenomenon are reliable and bear strong scientific validity, since the same or similar results would have arise by the use of two different scientific methods.

Only a limited number of *field experiments* have been attempted in this scientific field. In cooperation with the competent authorities are collected data for the taxpayers in order to identify their behavior towards tax evasion. The main reason for the scarcity of scientific studies of this type is the high cost of organization and coordination between the administrative authorities and researchers, something which does not exist in a laboratory experiment. A further obstacle to conducting this type of research is the fact that disclosure of tax data is prohibited by some jurisdictions, as these consist of sensitive information, not allowed be disclosed to third parties.

The method of questionnaire survey is currently the most frequently used in literature. The main reason of the widespread use is the lack of empirical numerical data. New empirical data that will be collected by the construction of the proper questionnaire will facilitate us in the assessment of the level of tax compliance and tax morale, while by using appropriate scientific methods will be identified the main factors that influence it.

The overwhelmingly large number of investigations in this field of research has been carried out by the economist Benno Torgler (in Queensland University of Technology Business School, Economics and Finance), either exclusively or in collaboration with other leading researchers such as James Alm (Tulane University), Bruno Frey (University of Zurich) and Friedrich Schneider (Johannes Kepler University of Linz).

The U.S. is leading in the research of tax compliance and tax consciousness. Studies have also been conducted in other countries, mainly in Europe and Latin America. The purpose of research is to, firstly, estimate the size of the tax morale and secondly to identify the social and demographic variables that mainly affect it. In some of these studies the degree of correlation between tax ethics, informal economy, tax evasion and corruption is examined. Each survey focuses on those variables that are considered important for the country (or countries) under research. In the following paragraphs we will briefly mention some empirical research related to the subject and the main conclusions reached.

4. SUMMARIZED LITERATURE REVIEW

1. A questionnaire survey has been conducted in the case of Austria by Torgler and Schneider (2005), who used data from the World Value Surveys for the periods 1990 and 1999. According to the survey results the country's citizens have indicated, in comparison with other European countries, a very high degree of tax morale, which increases when the confidence of citizens in the laws and judicial system is higher. Moreover, the high national spirit and religious beliefs positively affect the tax consciousness. Equally important is the variable "Perceived tax evasion» which is negatively correlated to the tax morale.

2. Torgler (2003), wondering whether there is a correlation between tax evasion and tax morale, conducted a relevant research in the U.S. The results indeed indicated a very high degree of negative correlation between the two variables, as also supported by theory, but can also lead to the conclusion that the investigation of tax morale can facilitate the identification of factors that affect tax compliance (and its opposite, tax evasion) and the degree of influence. Using the questionnaire survey results it is supported that tax morality is higher when there is trust in the operation of the government and other institutions and laws, when citizens are treated with fairness by the tax system, and when there is a sense of participation in decision making. Proper questions which reveal the preferences and level of tax ethics of individuals were used as proxy variables.

3. In a survey conducted in the U.S. and Europe by Alm and Torgler (2006), it is attempted a comparative analysis of tax morale among people living in the U.S. and Spain. The results indicate a significantly higher tax consciousness of the U.S. residents compared with those of Spain. Expanding research in 14 more countries in Europe, it is found that Switzerland and Austria also exhibit very high tax consciousness. Finally, a strong negative correlation between the shadow economy and tax morale is observed.

4. In a survey conducted in Latin America by Torgler (2004), it is attempted a first assessment of tax morale of the inhabitants of the countries of Central and South America. To carry out the study, sample questions were extracted from the material in the WVS extensive questionnaires and Latinovarometro, previously addressed to residents of all countries. The analysis proceeded in the assessment of negative correlation between tax ethics, shadow economy and corruption. In a next step, by setting tax morale as the dependent variable, Torgler considers whether and how this is influenced by the perception of respondents on various issues such as the extent of tax evasion (perceived tax evasion), the possibility of tax audits and trust in government officials. In this way it can be verified whether the tax morale is influenced by factors that are supported by the theory.

5. In empirical research conducted by Frey and Torgler (2007) using data from Eastern and Western Europe, it was found that tax morale is reduced where there is a perception that tax evasion is widespread.

It is evident from the above empirical research that the vast majority of data used is retrieved from institutions with long experience and international recognition such as the World Values Survey, the European Value Survey (EVS) and Latinovarometro. The World Value Surreys (WVS) is a global research organization that examines the social, cultural and political factors and changes occurring in various countries. To achieve its objective is based on the submission of questions to a representative sample covering at least 1,000 people in each country. The surveys take place through face to face interviews in respondents' homes and in their native language. The European Value Survey is also a research organization that focuses on research within the European countries, while Latinovarometro focuses on research carried out in countries of Central and South America.

5. EMPIRICAL RESEARCH IN GREECE

Tatsos (2001) has performed in the case of Greece research with the use of questionnaire survey. Through the construction of a questionnaire four indicators were formulated: Index of Tax Evasion, Tax Ethics Index, Index of Tax Justice and Index of efficiency of tax collection services. An attempt to identify the factors that act as a deterrent to tax evasion and enhance tax morale was based on the use of an econometric model in which tax evasion and tax ethics were treated as dependent variables. As explanatory economic and fiscal variables were mainly the probability of tax audit, the tax penalty, and the discomfort caused by the time consumed in a tax audit. Factors that act as deterrents to tax evasion included the following: low level of income, high tax penalties, high frequency of tax audits, reduced tax rates and the conduct of tax audits.

Regarding the tax ethics, research indicated that is significantly affected by the occupation. Employees and retirees present higher tax consciousness in relation to people of different activities. On the negative aspects of the empirical research were (a) the limited number of qualitative-social variables used in identifying the factors that affect tax morale, while those utilized (such as the tax justice and the way the management of public revenues is performed) were not found statistically significant; (b) there is an implicit assumption for the existence of a linear relationship between independent and dependent variables by using the method of least squares, in contrast with the other international empirical investigations aforementioned, since most variables are of qualitative type. It is also difficult to draw conclusions on tax variables such as the amount of tax penalties or the frequency of tax audits with the formulation of simple questions to citizens. It is expected to confirm the question that in their opinion raising e.g. the tax penalties will decrease tax evasion. In this way it is not indirectly inferred any information capable of further scientific processing.

6. PRELIMINARY RESULTS FROM OUR RESEARCH

The preliminary qualitative data of our interviews and pilot tests conducted under the THALES Programme indicate that because Greece's GDP has fallen due to the recession in the period 2008-2013 by approximately 25% cumulative, the loss of income experienced by Greek citizens has led to an increase in the number of actions of corruption, contribution evasion, undeclared employment, tax evasion, and unrecorded transactions in general. However, and as might be expected, the average amount of money involved in corruption in all these cases has decreased. Therefore, for example, although the Corruption Perception Index (CPI) ranks Greece among the biggest Corruption Perceptions Index improvers in 2013, the deterioration of disposable income and living standards, and the perception that the financial scandals and corruption by highly ranked Government officials has led to the debt crisis, and the rigid fiscal measures undertaken in turn, all these have made the authors of this paper, based on the first results of our research, to disagree with the conclusions of the CPI. Instead we can argue that the level of tax morale in Greece during the crisis has worsened due to the lower living standards and the severe Greek sovereign debt crisis, and Greek citizens try to replace the loss of income by tax avoidance transactions, contribution evasion by employers and employees for Social Insurance and other-Auxiliary Funds for Employees, and concealment of income.

Considering the above, the prevailing pattern or typology characterizing the typical Greek taxpayer, particularly during the current period, can be explained to a certain extent by the conditional cooperation paradigm, but also, secondarily, by the low intrinsic motivation. It can be argued that this results from dissatisfaction to government’s policies and tax administration actions, and the perceived increasing tax inequality, whereas the feelings of anger or injustice tend to reduce the moral costs of evasion and to engage people more in tax evasion activities in order to restore equity.

On the other side we find that the strict control mechanisms and electronic governance (e-governance) have contributed to the reduction of corruption associated with tax evasion and social security contribution evasion, due to the risks and penalties associated with the higher possibilities of detection and the increased number of tax audits and inspections carried out. As a result, and in contrast to the reduction of the shadow economy as a percentage of GDP from 28% before the crisis at 24% in 2013, as released by other Researchers (Bloomberg, Schneider), we estimate that at the end of our full research analysis, probably, this percentage will have exceeded 30% in 2013/2014. Finally, comparing the relative significance and sizes of tax evasion, as also revealed by the high percentage of shadow economy, and tax avoidance, which concerns mostly the self-employed and enterprises, it could be argued that the problem of tax evasion and fraud is larger in terms of magnitude, as also discussed in the next section.

7. SIZE OF TAX EVASION AND AVOIDANCE AND SOME POLICY CONSIDERATIONS

Tax fraud and tax evasion are limiting the capacity of the Greek government to raise revenues and to carry out its economic policy. Estimates show that billions of euros remain often unreported and untaxed, reducing national tax revenues. Decisive action to minimize tax fraud and tax evasion could generate billions in extra revenue for public budgets in Greece and across Europe.

Tax fraud and tax evasion are also a challenge for fairness and equity. Fairness is an essential condition to make the necessary economic reforms socially and politically acceptable. The burden of taxation should be spread more evenly by ensuring that everyone, whether blue-collar employees, multi-national companies that benefit from the single market or wealthy individuals with offshore savings, contribute to public finances by paying their fair share. Fairness and equity also mean creating better and fairer taxation systems.

As an example, in Greece, many are those who argue that tax revenues of hundreds millions of euro a year are lost by the Greek government from illegal activity such as in fuel trading, arguing that tax evasion and fraud affect both public revenues and healthy companies. Experts say that specifically fraud, piracy, incomplete deliveries to consumers, lack of transparency, the limited fraud inspections, delays in sentencing, fictitious exports, the lack of controls for maintaining buffer stocks substantially all arise from the luck of proper control mechanisms set by public authorities. Further, it is noted that the existing institutional framework is inadequate to eliminate the barriers in competition and healthy functioning of the market and achieve consumer protection (Bitzenis and Kontakos, 2014).

Particularly, smuggling in shipping oil sector remains important. Tax-exempted allocation of shipping fuels is required by the provisions of Articles 15 and 23 of Law 2127/93 and Law 603/77. The supply of passenger and cargo ships is carried out by tank cars, transporting untaxed fuel (transit). The smuggling process is based on the so called "slepia", i.e. small tankers which load the marine fuel from refineries, in customs’ presence, stating that the amounts are intended for the refueling of ships. The surveillance mechanism of this activity on the part of state authorities remains inadequate and important measures remain to be undertaken in this direction (Bitzenis and Kontakos, 2014).

In a single market, like the Greek one, within a globalised economy, national mismatches and loopholes are too easily exploited by those that seek to escape taxation. Indicatively, we can refer to the recent case of the oil marketing company ETEKA S.A., who was accused in February 2014 for illegal marketing of 4.5 million litters of shipping oil, and evaded customs duties and taxes that exceeded EUR 3.5 million. Among stakeholders were also owners of service stations, oil company executives and staff of the Ministry of Environment. The total oil consumption of shipping oil is about 713,000 cubic meters and according to sources market smuggling in this form corresponds to approximately 20-30% (Newpost.gr, 23/2/2014; Capital.gr, 2/11/2011). Mardas (2014), estimates that the total loss from illegal trafficking of fuels approximates EUR 2.5 billion annually (Naftemporiki, 22/2/2014).

The size of shadow economy in all EU Member countries is estimated at almost 2 trillion euro total or one-fifth of GDP on average. Tax evasion and avoidance have a significant cross-border dimension and form a complex problem that requires a coordinated and multifaceted approach by the EU and are global challenges which no member country can face alone, even if there is political will. Individual national efforts to address this problem will not work because we live in a globalized economy where national mismatches and “windows” (loopholes) are tools for those seeking to evade taxes despite the existence of technological progress. So at a national level, member countries need to improve their administrative capacity and the ability to collect taxes, but there should be also an administrative cooperation between member countries.

Particularly, Greece is generally characterized by a) instability in the legal framework with frequent changes in the laws, b) failure to implement laws, c) discrimination in law enforcement and/or the sanctions, d) lack of transparency in the application of laws e) lack of appropriate laws, f) the existence of " windows " in the implementation of laws, g) bureaucracy h) lack of significant penalties deterrent to any law violation and illegal action, i) bribery and corruption in law enforcement, j) lack of control mechanisms or lack of existence of fair control mechanisms, and k) there are facts which give space for bribery, corruption and bureaucracy (Bitzenis, 2009).

In Bitzenis, Schneider and Vlachos (2013) corruption and bureaucratic inefficiency amount to a tax on all firms that operate in Greece’s formal sector. A recent OECD (2011: 83-86) Survey[2] indicates that inefficient tax collection and the size of tax evasion is due to activities in the realm of the shadow economy together with bribery and corruption result to losses of fiscal resources between 2-4 percent of GDP per annum. An increase in tax revenue, which requires a great deal of reforms both in the efficiency of collection and in combating tax evasion, is necessary for the consolidation needed to place the public finances on a sustainable path. The reforms required are explicitly related to personal income tax, e.g. the self-employed declare incomes near the minimum taxable threshold. Of equal importance is also the inefficiency in collecting the VAT and social security contributions. The often annual practice of tax amnesties adopted by Greek governments is likely to have encouraged people not to pay taxes when they are due as the expected penalties are low.

Low tax morale and mistrust in public institutions is still a major cause for the inability of fiscal authorities to meet projected tax receipts. Tax morale in Greece is not only related to mistrust in public institutions. This form of tax morale, which has been frequently termed by the Greek media as the "sport of tax evasion", describes the norm of evading taxes for personal gain and can be understood through the absence of a "social norm" of tax compliance. Although tax administration improvements and strict tax enforcement can lead to higher levels of tax morale, nevertheless significant improvements will materialize in the long-term. Since the level of tax morale is greatly affected by the efficient use of resources in the public sector, it would be difficult to have considerable improvements in short-term. In view of the fact that the Greek crisis has also political dimensions (i.e. rent-seeking) and the inefficient use of public resources is deeply rooted.

The cause for the tax evasion is also related to the existence of high rates and perhaps a factor that would assist tax evasion reduction would be the decrease of taxation rates and the lowering of the tax scales and a reform of the taxation system. The taxation system remains too complicated to be understood by taxpayers, and there is a continuous change which tends to surprise tax payers and creates adjustment problems. Also, the allocation of the tax weights is negatively progressive. As a result, although as per typical law violation behavior, new laws tend to generate initial gains for the government, as in the case of the newly introduced property and estate taxes, the efficacy and sustainability of these gains over time is highly questioned both due to lessening political will and increased public resistance. Further, the possibility of establishing a multi-period taxation scheme which in every successive period would require different regulations so that tax payers do not have a chance to "play" the system to their advantage (as, for example, in the case of the USA’s, where the inheritance tax systems and rates change every other two to three years) is of limited applicability or effectiveness, considering that the current Greek taxation system is characterized still by the lack of or has not reached yet a “steady-state” position, which would facilitate the introduction of more parametric attributes from advanced taxation systems.

8. CONCLUSIONS

The paper reviews the main methodologies used by empirical research in assessing the levels of tax morale and compliance, such as laboratory experiments, surveys and field reviews. The empirical evidence from research that has been contacted in Greece and internationally is summarized. From the review performed a significant gap of comprehensive empirical research can be observed in the case of Greece.

Preliminary results from a questionnaire survey currently performed in Greece by the authors are presented. According to these first results, there is evidence that the level of shadow economy in Greece has increased in the period of economic crisis, and particularly during 2010-2013, in contrast with the indications of other relevant research and international published indicators. The prevailing type characterizing Greek taxpayers’ behaviors can be approximated by that of the “conditional cooperator”, of whom the attitude is driven primarily by a perceived sense of inequity, and the propensity towards tax evasion activities to restore equity, whereas frustration with institutional factors, such as e.g., the actions of government or tax administration authorities, tend also to further undermine tax morale.

Finally, selected policy considerations were discussed, related particularly with the size and causes of tax evasion and tax avoidance in Greece, and, indicatively, in the shipping oil sector. As the authors argue, the Greek taxation system remains still very complicated and under continuous adjustment, particularly in the light of recent restrictive measures imposed by the Troika and the Greek's government efforts to enhance revenues and sustain public debt.

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ENDNOTES

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2. The issues of the shadow economy and tax evasion have also been the subject of past OECD surveys on the Greek economy (see OECD, 2009: 58-65).

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