

## Chapter 64

# Taxpayers' Attitudes towards Tax Evasion in Latin American Countries

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### ABSTRACT

*The weight of the state in economic and social life is very important even if it might differ from country to country. The state provides particular public services and needs to the various funding sources to provide these services. Taxes constitute the largest share of financial sources needed by the state to operate effectively. However, taxes are often not welcomed by taxpayers, creating the unwanted behavior of tax evasion. The purpose of this chapter is to reveal the tax structures of Latin American countries and to examine tax morale as an important determinant in shaping the attitudes of taxpayers in Latin America. This chapter shows the most important component of tax revenues in Latin American countries constitutes consumption taxes instead of income taxes, in contrast to developed regions such as those in OECD countries. It shows the tax structure in Latin American countries reflects the typical tax structure in developing countries. It is also observed that average tax morale is higher in South American countries, such as Venezuela, Paraguay, and Argentina, than in other areas, although it has a changing property over time. Moreover, the chapter shows tax morale is associated with financial indicators (satisfaction with income, the present economic situation, income distribution, and the functioning of the market economy), policy indicators (satisfaction with democracy, confidence with government), and demographic indicators (age, education).*

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## INTRODUCTION

In its simplest form, tax can be defined as an economic obligation imposed by the state on natural and legal persons. Taxes which are a share of individual to public expenditure necessarily are the main source of income for countries all over the world. However, Alm, Martinez-Vazquez and Schneider (2004) state that most people do not like to pay taxes and that tax authorities have difficulty imposing and collecting taxes. Therefore, for all countries tax evasion remains a serious challenge facing income tax administration and hindering tax revenue performance. One of the most important problems especially in developing countries is the social, political, and administrative difficulties in establishing a sound public finance system. As a consequence, developing and emerging countries are particularly vulnerable to tax evasion and avoidance activities of individual taxpayers and corporations (GIZ Sector Programme Public Finance, Administrative Reform, 2010).

Widespread tax evasion in developing countries has a major effect on local economies (see de Soto, 2000). A high degree of tax evasion creates misallocations in resource use (Alm & Martinez-Vazquez, 2001). Such a high level of tax evasion also reduces a government's ability to work and provide adequate services. Therefore, governments in all countries, especially those in developing countries in which the tax system is not fully established, attempt to develop policies and take measures to ensure tax compliance. An important discussion in tax compliance literature is why individuals pay tax. Theoretically, the extant literature has provided evidence suggesting that tax compliance can be influenced by numerous factors. In the tradition of tax compliance approach (the neoclassical model of tax evasion) as developed by Allingham and Sandmo (1972), individuals evade taxes as long as the payoff from tax evasion outweighs the costs of being

caught evading tax responsibilities. Therefore, increasing the costs of tax cheating or increasing audits and harder penalties for tax evasion would potentially reduce tax evasion.

Although the traditional of tax compliance model has been argued in terms of its simplicity and specific policy predictions, the model has fallen short of explaining why observed levels of tax compliance in real life are higher than theoretical predictions. The basic criticism is that the traditional of tax compliance model ignored the role of individual attitudes towards compliance with taxes. This has motivated researchers to develop new models of tax compliance which can better explain the complexity of tax compliant behavior (Alm, 1999). Beyond audits and penalties, there are also many non-economic factors affecting the level of tax compliance. One of the most important factors within non-economic considerations is tax morale. It has been well-established that taxpaying behavior cannot be explained in a satisfactory way without considering tax morale (Frey, 2003). Tax morale in tax compliance has considerable influence guaranteeing an adequate provision of public goods and generating revenues in times when the costs of running public office have strongly increased.

The main purpose of this study is to show tax structures in Latin America countries and to consider the attitudes of taxpayers towards tax evasion in these countries. Therefore, in Section 2 we will make comparisons between countries by showing basic indicators about taxes in Latin America countries. Section 3 provides a summary about tax compliance models in the extant literature. Section 4 provides a general overview on the concept of tax morale and the role of tax morale in shaping tax compliance behavior in Latin America countries. Section 5 presents tax morale level as a determinant of tax attitude of taxpayers in Latin America countries. The chapter finishes with some concluding remarks.

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