Corruption, Complexity and Tax Evasion*

By

Vito Tanzi**

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** Vito Tanzi, an economist, is Honorary President of the International Institute of Public Finance. He served as Head of the Tax Policy Division and as Director of the Fiscal Affairs Department at the International Monetary Fund. He was also Undersecretary for Economy and Finance in the Italian Government and President of the International Institute of Public Finance.

I. Introduction

Corruption is an old human activity. References to it go back thousands of years. In the distant past, corruption had not always been considered an illegitimate or undesirable activity, and some modern societies continue to be relatively indifferent, or at least more tolerant, of it than others. It was during the high days of the Roman Republic, when a modern legal system started to be created, that made corruption an undesirable and illegitimate activity. Centuries later, Dante, the great, Italian, medieval poet, in his literary masterpiece, <u>Inferno</u>, would place corrupt people in the deepest and most painful levels of Hell.

The term comes from the Latin verb "to break", because it is assumed that corruption breaks some widely accepted norms. The term seems to have entered the English language at about Dante's time, in the 13th-14th Centuries. A few centuries later, the American Constitution made corruption, together with treason, one of two explicitly - mentioned crimes that could lead to the impeachment of an American president.

Over the years there have been various and different definitions of corruption, some more morally- based and some more legally-based than others. The concept of corruption, defined as *the act of breaking an accepted social or legal norm*, must inevitably recognize that different societies respect different norms, and that some norms are not precisely defined. Therefore, an act that may be considered corrupt in one society may be seen as normal, expected, or tolerated in another. This is especially the case when the act reflects relations with, or assistance provided to, friends and family, or to other members of close communities. In some societies, for example, exchanges of favors, that may hide bribes, are considered normal. As a consequence, some forms of corruption take the form of or start as favors. Tanzi, 1995a.

In recent years there has been the problem of the rise of what could be called *legal corruption*, that is behavior that many may consider questionable or even illegitimate, but that is not explicitly forbidden by a specific law or regulation. Examples of legal corruption have come from the financial market, from some forms of tax-avoidance, and in some mineral exporting poor countries from some questionable acts on the part of policymakers.

The above means that the role that culture plays in human relations is important in understanding why corruption continues to be more common in some parts of the world than in others. Ibid. For this reason, much time was spent in international meetings, during the decade of the 1990s, when corruption had become a significant global issue, due to globalization, and it had become necessary, for lawyers from international organizations and from countries, to agree on a legally agreed, definition of corruption. That definition would apply to all actors operating in a world that was becoming progressively more globalized, and when multinational enterprises and individuals were increasingly operating in places with different cultures and different legal systems.

Tax evasion is a slightly more recent sin than corruption. The term also first appeared in the late Middle Age and was linked with the taxing activity of the governments of "city –states". It refers to illegitimate actions on the part of taxpayers directed at evading the payment of due taxes. A modern day visitor to Venice can still see, at the entrance of the Ducal Palace, in Piazza San Marco, an old, carved stone that, centuries ago, had invited Venetian citizens to report those who were hiding taxable activities from the Republic of Venice.

Both corruption and tax evasion, however defined, are, therefore, not just modern activities, and for many past centuries they have generally not been condoned. However, some experts have, at times, tried to justify them on various grounds, generally on grounds related to presumably bad laws and to the bad behavior of governments and policymakers. Some have argued that oppressive taxes may lead to and may thus justify tax -evading reactions. Very low wages may also justify some acceptance of bribes and too strict regulations may justify ignoring them.

As government activities grew over the years, and as they required higher tax revenue, more public spending, and more government regulations, both corruption and tax evasion seemed to grow and to become more widespread in the modern world. Tax evasion had attracted some attention of economists for some time but, until the decade of the 1990s, corruption had attracted much less attention by them. Until that time, references to corruption had come mainly from political scientists, historians, or even from opera composers (see Manon Lescaut, and Tosca), but not from many economists. However, starting in the 1990s corruption has been receiving a lot more attention from economists than earlier.

This paper discusses reasons for these developments. It argues that they are likely to rest on both the growing public activities of governments and the growing complexity of modern government operations.

II. On Tax Evasion and Corruption

After World War Two, there were two major developments, worldwide, that called for higher tax revenue, in both rich and poor countries. Rich countries were abandoning the more *laissez faire,* or low government spending, policies of the past, and had started on a path that would transform many of them, within a couple decades, into modern welfare states. Or, at least, that they would create new and expensive government programs, even in countries that would not become classic welfare states, as for example the USA, Australia and some others.

To finance the higher public spending, the rich countries' governments needed additional revenue. The needed resources came, first, from a greater use of income taxes and from many, assorted, small taxes; successively, they came increasingly from the newly introduced value added tax, or from some other kinds of general sales taxes. Income taxes and value added taxes became the two major contributors, over the second half of the 20th Century, to the rise in tax revenue in industrial countries. They explain much of that rise.

During the 20th Century the average tax level in the industrialized countries would increase from around ten percent of GDPs, the average level at the beginning of the century, to over 30 percent of GDP, by the end of the century. In several European countries, the tax level would even exceed 40 percent of GDP. In most OECD countries, the growth in tax levels would come to a stop in the new millennium. More recently pressures have built that are pushing for tax reductions, in several countries.

After World War Two, many poor, developing countries, had come out of their former, colonial status and had become independent. Their governments were soon confronted by statistical evidence, made available mostly by the statistical offices of the United Nations and the newly- created Bretton Wood institutions, that quantified the rather obvious conclusions that these countries were much poorer than the rich countries. They badly needed to adopt policies that would make their economies grow, to begin a process of conversion with the rich countries' living standards.

Development economics was then becoming an important field of economics and many development economists had concluded that the governments of the developing countries should play a leading role in the economic development of those countries. At that time there was a lot of confidence in what good governments could do for their economies. Most economists were convinced that economic growth could not be expected to originate spontaneously from the actions of private sectors, that, at that time, were far from modern.

The development strategy that was recommended by many economists was: (a) the developing countries needed to accumulate more capital; (b) the governments had to raise the countries' tax burdens, to have more resources available; (c) they should keep government current spending low; and (d) they should use the budget surplus thus generated to build badly needed public infrastructure and to accumulate capital.

At that time, economists' model considered capital accumulation as the key ingredient to generate economic growth. The *capital -output ratios* and the *tax levels* became two development statistics that attracted much attention, and taxation was seen as central in the promotion of economic development. Most developing countries were urged to increase their tax levels with adequate tax reforms and with foreign technical assistance. Foreign aid could add to the government available resources.

Econometrically –based estimates of the *tax potential* of countries became important policy inputs. Tax rates were pushed up and new taxes were introduced, to raise the tax levels. However, because of tax evasion (and the opposition to high taxes by the citizens who had more taxable capacity and political power), assisted or facilitated by corrupt tax administrations, tax revenue generally increased far less than hoped. Corruption also entered in investment decisions, making capital less productive. See Tanzi and Davoodi, 1998.

III. Factors Contributing to Tax Evasion and to Corruption

Some real -life examples of tax evasion in particular developing countries may help give a feel for the importance of the problem. Examples from two important Latin American countries, Argentina and Peru, will be used. They are borrowed from two books: Tanzi, 2007a, pp. 30-33, and Tanzi, 2010, Chapter 8. Similar examples could have been taken from Asian countries.

In Argentina, by 1975-76, the share of tax revenue into GDP had fallen sharply, to well below the already -low level that it had averaged over previous years. Several factors, relevant to our discussion, had contributed to that fall. At that time there was also the role that high and increasing inflation, combined with delays in the payment of due taxes, can play in reducing real tax revenue. That particular factor, that came to be described in the economic literature as the "Tanzi effect", will be ignored in the discussion that follows, because it is not relevant, especially in these non- inflationary times. See Tanzi, 1977.

First, and quoting from page 31 of Tanzi, 2007, the tax administration of Argentina "…had become a relaxed place where many employees received full-time (though much compressed real) salaries but worked for only few hours a day. Many…had private practices where they spent much of their working day advising the same taxpayers they were supposed to be administering [in their official jobs], on how to reduce their tax liabilities. Some were corrupt and, for a bribe, would take care of the tax problems of some taxpayers. They would use their power in the selections of audits, in the determination of fines, in the intentional misplacing of relevant files, in selecting taxpayers for inspections, in estimating the incomes or the sales of taxpayers and so on. Some…. would accommodate requests from politicians to go easy on some taxpayers…. As one employee put it: you interpret the law for friends and apply it rigidly for others".

The above paragraph conveys a lot of information on factors that can contribute to tax evasion, and on the role of corruption and other factors to encourage, facilitate, or make tax evasion possible. The cited book on Argentina contains also information on strategies that taxpayers used to evade taxes [faking invoices, not reporting incomes, and so on], in an economy that was still close and where *global tax evasion* was not yet playing the major role that it would come to play in many countries, in later years. See pp. 32-33. One exception was the actions of some rich Argentines who deposited their money in US banks where, as deposits made by "non resident aliens", the interest earned on the money deposited was not taxed by the US government and was not reported to the Argentine tax administration. In those years tens of billions of US dollars, belonging to Argentine citizens, were deposited in US banks.

In the Peruvian case, reported in chapter 8 of Tanzi, 2010, Alberto Fujimori, a shy, agricultural economist of Japanese background, who, in a surprising election, had been elected president of Peru, in 1990, had invited the IMF to assist his country with the collection of taxes. At that time the tax level of Peru had fallen to about seven percent of the country's GDP, and Peru was in arrears in the payment of salaries to public employees, or in the servicing of its foreign debts. The main reason for the drastic revenue fall had been that the tax administration had become totally disfunctional and corrupt, during the years of the leftist, populist, government of Alan Garcia.

The tax mission that the IMF sent to Peru, to study the problem, after a few days of work, reached the conclusion that the Peruvian tax administration was just too corrupt to be reformed. Drastic surgery was needed. As the book put it, "[i]t was necessary to shut down the existing tax administration, sending home most of its employees, and to create a new one, from scratch. The new administration would have a salary structure comparable with that of the Central Bank, but the new employees would not enjoy tenure in their jobs. They could be fired at any sign of corruption, or of incompetence". Tanzi, 2010, p. 94.

A new administration, staffed mainly with carefully selected recent college graduates, was created. "Within a short time, the situation began improving significantly, [tax revenue went up], and the new administration…was able to move into a new building." Ibid, p. 95. An incentive system was created that allowed the tax administration to keep a certain share of the total revenue collected, to allow it to pay bonuses for top performers. Some of the managers of the new tax administration came from the central bank.

The above descriptions, of specific experiences of two Latin American countries, make it possible to identify and to comment on factors that play, or can play, important roles in the tax evasion of most countries.

Some of these factors are:

(a) *The role of administrative controls*. All public institutions need some effective controls to operate efficiently. There is no "invisible hand" that can make them operate without controls. In institutions with weak or no controls, the employees spend less hours working than the official office hours suggest they should. Furthermore, while at work, many work at a slow pace. Extended coffee breaks, frequent visits to restrooms, long lunches, frequent absences from the offices, because of faked illness or other excuses, and, while in the offices, trivial conversations with colleagues, and other actions can take a toll on efficiency and productivity.

(b) *Inefficiency and absenteeism* that inevitably affect performance. Recently, in Italy, there have been many reported cases of employees who, in the morning, checked in their offices and, as in Argentina in the 1970s, disappeared for a good part of the day. *Job tenure* had made it difficult for the government to fire those who got caught. In some cases employees had established reciprocal arrangements with colleagues, who would electronically "card in" their arrival.

(c) The "presence" of "*ghost workers*", workers who receive salaries but never show up for work, or may not even exist.

Poor accountability, political corruption, and slack controls make possible the payment of salaries to *virtual* employees. In both of the above -described situations the need for controls *internal* to the institutions, and also for controls by *external* government -wide institutions (such as General Accountability Offices, or Courts of Accounts) are important. In recent years this aspect has attracted more attention than in the past, in several countries.

(d) The *salaries' levels.* This factor has received empirical support in some studies. When salaries are low, there may be a greater temptation (or need) for some employees to accept bribes, or to engage in other illegitimate activities that generate some incomes to them. This had happened in both Argentina and Peru. Low salaries, combined with job tenure, are factors likely to promote bad incentives.

(e) Government salaries *kept low salaries* on the very assumption that the workers are receiving bribes that increase their incomes. The reasoning is that, because of the bribes, the government does not need to pay higher salaries. This attitude ends up legitimizing corruption and justifying the acceptance of bribes.

(f) *A salary structure* that prevents some necessary and justified differentiations in salaries, between individuals with greater ability, initiative and responsibilities and others. When the salary structures become too flat, they are likely to lead to poorer performances and to other difficulties, especially when the better trained and the top performers have the option of quitting and working for private and often foreign corporations, at higher salaries. This drainage of talent has become a more common problem, in recent years, in many developing countries, because globalization has brought potential foreign employers to countries.

(g) *The impact of rigid Job tenure.* When individuals cannot be fired, at times even for incompetence or for some corrupt acts, job tenure ends up encouraging those acts. Labor unions generally defend job tenure, and some job security for public employees is obviously important, to prevent politically motivated or abusive firing. In recent years, some countries have traded the freedom to fire unproductive or corrupt workers against higher salaries, as Peru did in the 1990s.

(h) The *cultural dimension*. It was mentioned earlier that *corruption has a cultural dimension.* In some forms, as with the exchange of favors that at times may hide bribes, or with assistance to relatives, it is more condoned in some cultures than in others. See Tanzi, 1995a. For this reason it may tend to be a greater problem in sub national governments, because of the greater proximity of individuals who know one another, or that are related. Corruption can also take aspects that are more difficult to notice. For example, how quickly, or how favorably, an employee responds to a request from a citizen who needs some government authorization may depend on personal connections with that citizen.

(i) *The role of contagion*. Corruption *may be more contagious in some cultures* than in others. When some employees engage in corrupt acts, others may be more likely to denounce them, or to imitate them. This may depend on cultures and possibly on tradition. Therefore, specific rules and active controls against some actions may be more necessary in some countries than in others.

(j) Some economists have ignored or removed the cultural or moral element from acts of corruption or other crimes and have made individual decisions, on weather or not to commit a crime, depend mainly on *the probabilities of getting caught and on the expected penalties expected* if caught. See Becker, 1968, and Allingham and Sandmo, 1972. See also Chalfin and McCarry, 2017 for a review of related literature. While the above factors are clearly important, the moral attitude of individuals vis -a -vis some illegitimate, or illegal, actions must also play a role and should not be removed from these decisions.

(k) *Unnecessary discretion in some actions,* such as the choice, by tax administrators, in the selection of taxpayers for audits; in the determination of the size of some fines; in the granting of tax incentives, and so on. Discretion in some actions can encourage acts of corruption. The granting of incentives has been a problem in several countries, especially in Asia. This implies that discretion should be limited, and that administrative decisions should be based, as much as possible, on specific and precise rules. When that is not possible, there should be more strict ex post controls. Naturally, total absence of discretion may not be desirable and might create occasional problems because some situations that require judgment and discretion.

(l) *Relations between tax administration and politicians*. Political influence on tax administrations remains a major problem in many countries, especially in developing countries. The insulation of tax administrators from the interference of politicians is thus essential to prevent corruption and tax evasion. There has been a lot of attention over the years to the need for the political independence of central banks, but not enough about the need for the political independence of tax administrations.

(m) The *absence of incentives,* beside the general level of salaries, for encouraging efficient performances of employees. Criteria for hiring, promotions, and salary increases are obviously important. Policies that end up rewarding good and bad performances equally are more likely to lead to corruption.

(n) *The appointment* in high- level administrative positions of *politically connected individuals* with the power to channel to them the handling of some corrupt, but politically supported, acts. This happened in Peru, in the later years of the Fujimori administration, when a corrupt colonel was appointed as a deputy head of the tax administration. Political acts of corruption were channeled through this individual. In time they created new, great difficulties for the Fujimori government, and for Fujimori himself. See Tanzi, 2000, p 120.

(o) Finally, in some countries, *corrupt policymakers* who may take actions, especially connected with the export of mineral resources, or the granting of attractive tax incentives to foreign corporations, that benefit the policymakers and not the countries. The media have reported on some of these cases in particular countries. This form of political corruption is more difficult to deal with because, in some sense, corruption has become legal.

The above list is long but, probably, it is not a complete list The importance of the mentioned factors is likely to vary from country to countries. Therefore, they should not be given equal weight, when assessing their importance in the incidence of corruption and tax evasion in different countries. Not all of these factors have received the attention by economists that they may merit. They largely describe institutional weaknesses. Many institutional quality indexes now available from the World Bank and from other institutions show significant correlation between growth and those indexes. One of them is control of corruption.

IV. On Tax Complexity and its Impact

There is now a lot of anecdotal evidence that indicates that corruption in the tax administrations and tax evasion and avoidance by taxpayers are facilitated by the complexity that characterizes tax systems and, to some extent, also tax administrations. Some tax systems have become so complex that few citizens can find their ways in the obscure jungle created by thousands of pages of tax laws and regulations. See Tanzi, 2013.

As a general topic for analysis and research, complexity has been attracting increasing attention by scientists, experts in particular areas, and economists. See, inter alia, Weaver, 1948; Waldrop, 1992; Heyndels and Smolders, 1995; Tanzi, 2007b; Mitchell, 2009; and Walpole, 2015.

Systems can be *simple*, *complicated* or *complex*. The working of a system that is *simple* is easy to understand and its results are generally predictable. *Complication* is the inevitable consequence of pursuing technically difficult tasks, such as going to the Moon, producing an atomic power plant, or building a modern jetliner or a smart phone. A *complicated* system needs many parts, and each part (say a battery) has some potential to fail, thus exposing the whole system to potential disasters. See Tanzi, 2007. However, the failures are specific and attributable to the parts. Apart from them, the internal working of a complicated system should be understandable and its functioning should be predictable to the experts who have built it. It should not be subject to randomness.

A Complex system is, in some essential ways, different from a *complicated* one. Complexity implies that a system is hard to understand

and to deal with. It may also be less stable. When a system is *complex*, its internal working and the way its parts are related to one another become less predictable. Some real life and especially technical systems inevitably need to be complicated, such as going to the Moon. They require the inputs of highly- trained specialists. Other systems, however, such as tax systems, can be complicated or complex. In these systems the human element is generally more important, and humans can be inefficient, corrupt and also irrational. When systems become complex, they become less understandable and especially less predictable in their workings and consequences.

In recent decades the tax systems of many countries became clearly complex, leading to the questions of whether complexity is a necessary evil for them, or weather it could have been largely avoided. See Walpole, 2015. The tax systems of some countries have become so complex that, in some concrete experiments, requests for clarifications, on how to deal with a specific tax issue, directed to different tax offices *of the same tax administration*, have received widely different replies. Furthermore, rather than interpreting some tax laws and running the risk of making serious and punishable mistakes, many taxpayers now prefer to pay tax advisers to prepare their tax returns. Assistance in tax preparations has become a big business in several countries.

Complexity is of course not limited to tax systems but is a characteristic that describes several systems in which humans play significant roles. In a forthcoming book, the author of this paper has argued that the growth of public sector's operations, over the past century--- a growth that was accompanied by higher and more complex taxes, higher public spending, many new government programs, and an increasing involvement by governments in the functioning of the countries' economies and in the activities of the citizens --- has created a lot of complexity in public sectors, and a fertile field for corruption, for tax evasion or avoidance, or abuses in some government programs. Tanzi, 2017,forthcoming.

How fertile tax systems have become for corruption and for tax evasion is likely to depend not only on the tax laws and on administrative arrangements, and on how effective are controls within the tax administrations, but also on cultural characteristics of countries.

Given the laws, the arrangements and the controls, some cultures seem to be more prone to condone corruption and tax evasion than others. See Tanzi, 1995a.

Complexity is often associated with the size of operations. Most human activities and institutions are more easily controllable when they are small. As they grow in size and in scope, they tend to become less controllable, and principal-agents problems grow. Take as a simple example the case of a small, family-owned and successful restaurant. Its success may convince its owners that it would be a good idea to expand it. They consequently rent a larger place, hire additional staff, add new dishes to the menu, and try to adjust the menu to the culinary tastes of the expanded and more diverse patronage.

The larger operation is likely to change the character of the operation and to bring difficulties that had been absent before. The incentives of the new, hired staff would be different. Principal -agents problems would be likely to develop. Some employees would be less dedicated and less responsible, than were those of the smaller restaurant, and so on. The new cooks hired may be less good and may have greater difficulties to satisfy the more varied tastes of the larger clientele. Organizational problems will require more controls and the adoption of clearer incentives, including greater use of penalties and rewards for the employees. In any case, uncertainty in outcome is likely to increase.

The solutions to the new problems are often not good enough to be able to cope with them, because of the greater complexity that size has created. And the greater *complexity has made the outcome less predictable*. The use of franchises or corporatization, a la MacDonald, and standardization of the product sold may reduce the difficulties in some activities and the uncertainty. In these cases the operation reproduces itself without adding complexity, as in a cloning operation.

Consider, next, tax systems and their administrations. Many years ago tax systems were simple, and tax administrations were small. The latter had to deal with simple and often “presumptive” or “forfeit” taxes. The taxes were not based on accounting but on cadastral values of land or buildings, on the frontage of houses, on the number of windows, on how much grain was taken to the mills to be processed, on the right to sell goods in the local market, or, simply, on the physical space that a shop occupied.

These simpler taxes, that required little discretion by tax administrators, were imposed on the taxpayers with *the sole objective of collecting revenue*. They largely satisfied a criterion, that had been given importance by the first Nobel Prize winner in economics, Jan Tinbergen: that each objective should be pursued by one instrument. In the past the only objective of taxation had been *to get revenue*. Like the famed Mao's tunics, the taxes used largely ignored the circumstances, or the sizes, of the individual taxpayers. Like poll taxes, one "size fitted all", because there was only one objective to satisfy.

Over the years, governments' needs for tax revenue increased and governments started to pursue other objectives in addition to collecting revenue. As the need for more revenue increased, and the objectives pursued became more numerous, new and more complex tax laws were introduced; equity and many other government objectives became important goals. The new taxes were increasingly based on accounting (income taxes, value added taxes, wealth taxes) rather than on the presumptive or forfeit criteria of the past.

New criteria were used for determining how much income tax a specific taxpayer should pay. The criteria increasingly took into account ability to pay, source of income, age of taxpayer, occupation, family status, size of family, use of income, and an increasingly large number of other considerations and social goals. The tax systems abandoned the Mao tunic's principle and, at least in intention, were attempting to fit an exquisitely-tailored Armani suit to each taxpayer.

The more governments relied on the tax systems to pursue an increasing number of social and economic objectives, the more complex the tax systems became, the greater were the opportunities created for some taxpayers to "game the system", and the less predictable their reactions. Increasingly this gaming was attempted with the assistance of "tax planners"; clever tax consultants; and, occasionally, in some countries, with that of corrupt tax administrators. As a random piece of information, the Italian Corte dei Conti (the Italian Accountability Office) recently estimated that in Italy there are now about 800 different tax "incentives", presumably pursuing 800 different objectives, through the tax system. In Brazil, the federal budget of 2016 had thousands of objectives to be promoted by it.

In many countries, the *level* of taxation became part of the problem, but it may not have been the main factor in contributing to tax complexity. Some countries have been able to raise high tax levels while limiting complexity (Denmark, Sweden and some others). They have done it by limiting special treatments, tax expenditures and many incentives.

Some other countries, especially but not only Eastern European countries, *introduced flat-rate income taxes* with the specific objectives of limiting complexity and the impact of higher tax rates on incentives. By so doing, these countries abandoned the important objective of *equity in taxation* and other potential objectives that many governments consider important in today's world. Also the introduction of *dual income taxes,* in the 1990s, by the Scandinavian countries was, to some extent, an attempt at keeping their tax systems simpler. See, Sorensen, 1998.

Taxes can still be progressive, in tax systems that are relatively simple, as in *dual income taxes*. However those systems must retain some features of Mao's tunics. They must avoid most of the special treatments connected, with income sources, personal conditions, and other objectives that most governments pursue with *tax incentives*, *tax expenditures*, *tax deductions* and so on. In other words they must ignore, all or most, particular conditions of taxpayers, except the income level. The dual income taxes manage to do that, to some extent, especially for taxes on capital incomes.

Value added taxes can also be kept simple, by having a single rate on as broad a tax base as possible. This is the secret for administrative simplicity, and for obtaining high revenue with lower tax rates.

However, in the pursuit of equity, many governments have continued to use multiple rates for different products, under the often mistaken belief that, by so doing, they achieve more equity. Various empirical studies of value added taxes have shown that this is a fiscal illusion. Often, the favorable tax treatment of what are considered "necessities" ends up benefitting more the higher income groups than those at lower income levels. It also makes the tax system more complex and promotes tax evasion, because it is easier to keep track of total sales than of the sale of specific categories of products and services.

The pursuit of higher tax levels, and especially of multiple social or economic objectives, has led to complex tax systems that, in some countries, have encouraged or facilitated tax evasion and administrative corruption. It may be worthwhile to cite the views of some tax experts, on the problem of complexity in some countries. These views were described in Tanzi, 2013.

Writing about the problem of complexity in the tax system of Australia, Margaret McKerchar, 2007, stated: "The Australian federal tax system is widely regarded as one of the most complex tax systems in the world…There is …scope to inflate…claims for deductions or to exploit the ambiguities created by complex laws and instructional material", p.192. Chris Evans and coauthors have more recently written on the complexity of the Australian tax system. See Tran-Nan, Lignier, and Evans, 2016.

On the UK tax system, in 1978, Kay and King wrote: "No one would design such a system on purpose, and nobody did. Only a historical explanation of how it came about can be offered as justification…of how seemingly rational decisions can have absurd effects in aggregate". This often results in complexity.

The Economist of April 16, 2005 cited a New Zealand report to ministers that had concluded that, the New Zealand Tax Code instills "anger, frustration, confusion, alienation".

When he was President of Italy, Eugenio Scalfaro, declared that the Italian tax system could only have been "designed by lunatics". If anything, continuous tinkering has made that system even more complex.

In the USA, a 2005 Report to the President underlined that ”tax preferences complicate the system, create instability, impose large compliance costs and can lead to inefficient use of resources”. When the US income tax was introduced, in 1913, it had 400 pages of laws and regulations. At that time some members of the US Supreme Court, that had to approve the new law, had already criticized it for its complexity. In the first 25 years of its existence the number of pages in the law grew to 504. However, by 2006 the law and related regulations had reached the extraordinary number of 66498 pages. See Edwards, 2006. In recent years the number of pages grew further at a fast pace.

Inevitably, complexity creates space for corruption and opportunities for tax evasion and tax avoidance. It also encourages the growing army of lobbyists to push for small tax changes advantageous to their clients, making the tax systems increasingly more complex. Complexity significantly increases the costs of administering the tax systems, and of complying with the many tax obligations for the taxpayers. These administrative and compliance costs are important “dead weights” on the countries’ economies.

A useful survey of many empirical studies, by Chris Evans, 2003, concluded that compliance costs can range between 2 and 10 percent of tax revenue, and up to 2.5 percent of GDP. Furthermore, they tend to be highly regressive. Additional estimates on these costs are available in Tanzi, 2013, and in Tran-Nam, Evans, and Lignier, 2016. These high compliance costs are often the direct consequence of complexity.

In addition to raising compliance costs, complexity may also contribute to instability, as mentioned by the Report to the President,

V. The Global Dimension

So far the discussion has ignored the impact that globalization has been having on the complexity of tax systems and on the related behavior by both countries and taxpayers. Both of the latter now operate in an open world and they must take into account the possible (positive or negative) impact on them coming from the tax systems of other countries. Countries can try to exploit possibilities created by “tax competition” and may even engage in “tax wars”.

While in the past tax evasion and related corruption had been connected mainly to *domestic* activities (often offered by the underground economy, by informal activities, and by inefficient or corrupt tax administrations), these behaviors have now, increasingly, gone global, at least for important taxpayers, such as corporations and "high net worth individuals" (HNWI).

Globalization has opened new doors and new opportunities: for countries' governments, to modify their tax systems, to better adapt them to an open world; and for individuals and corporations, who operate, or can operate, globally, to exploit the new tax avoiding possibilities created by globalizations. Now some governments attempt to export some of their tax burdens, and to import to their countries tax bases, from the rest of the world. Both corporations and HNWIs attempt to reduce their tax payments, by transferring profits or incomes to low or zero- tax jurisdictions, and by reducing their tax bases in high tax-rate countries.

In recent years globalization has been attracting growing attention, and so has its impact on tax systems. That impact has been associated with increasing tax evasion, growing tax complexity, and growing evidence of corruption, or other undesirable behavior, by the tax officials of some countries. Inter alia, see Tanzi, 1995b and 2012; and papers in Pogge and Mehta, editors, 2016. In May of 2016 the World Bank organized an important conference on "global tax wars" and soon it will publish a book on the topic. The OECD and the IMF have also been concerned with these developments.

By increasing multi countries and global economic activities of corporations and HNWIs, globalization has made tax collection more difficult than it had been. It has created new opportunities for tax evasion, for tax- related corruption, and for opportunities for some countries to take advantages of the existing global tax arrangements. In today's world, multinational corporations and HNWIs operating globally must deal with and can try to exploit tax-evading opportunities that global economic operations offer. Government can no longer ignore the impact that the tax systems of *other* countries can have on their countries.

Corporations have discovered that “global chains of productions” and the use of inputs (physical, financial, and intellectual) obtained from other countries can offer them opportunities to use “transfer prices”, “thin capitalization”, “patent boxes”, “secret or non transparent” arrangements with governments of “tax havens” or of “quasi tax havens” countries (Ireland, Luxemburg, Holland, Switzerland, Singapore, and even the UK and the USA), to reduce their global tax obligations, with tax avoidance, or with explicit tax evasion.

A fast -growing industry of tax advisers, accounting and law firms (such as that of Mossack Fonseca in Panama), and other tax “facilitators” is ready and willing to provide valuable assistance to both corporations and HNWIs on how to reduce their tax payments. See, inter alia, Palan, Murphy, and Chavagneux, 2013; Burgis, 2016; Pogge and and Mehta’; and Murphy, 2013.

The information that, in April 2016, came from the “Panama Papers” confirmed and provided interesting details to what was already known. It showed that a wide and often obscure (or “shadow”), global financial system, with the assistance of many banks and other financial institutions, and complicit government authorities can offer rich individuals opportunities to hide a large share of their income and wealth from tax collectors. This is often done by creating anonymous corporations, which become the legal owner of much of the world wealth; or in some other ways. See Zucman, 2015, for some estimates of hidden wealth.

There is not space in this paper to describe in detail some of the strategies that enterprises and individuals use to evade taxes. Available estimates of global tax evasion run into the hundreds of billions of US dollars. Papers in Pogge and Mehta, editors, 2016, and in World Bank, 2017, forthcoming, offer additional information and estimates of annual revenue losses to governments. A recent paper written by IMF economists has estimated losses of up to $600 billions. See Crivelli at al., 2016.

One important aspect of these global tax -avoiding operations is that they overwhelmingly benefit high net worth individuals. Therefore, they have contributed to the growing inequality in the distribution of income reported in many countries in recent decades.

Concluding Remarks

This paper has discussed *domestic* and *global* factors that, by making tax systems more complex, contribute to tax evasion and to tax related corruption. Similar arguments could have been made regarding the global financial system. That system has also become too complex for anyone to fully understand it. In addition to having become very complex, the global financial system is also influenced, perhaps more than the tax system, by the irrational behavior of those who participate in it as some recent literature has argued. To some extent, complexity has also characterized some government spending programs. See, Tanzi, 2007b and Tanzi, 2017, forthcoming. In important economic areas, complexity must have contributed to creating more uncertainty and more randomness in policy outcomes, raising the prospects of occasional unpleasant economic surprises, as was the financial crisis of 2007 and later years.

This paper has stressed that tax systems do not necessarily need to be complex. See also Walpole, 2015. Their complexity is a consequence of the roles that governments have increasingly wished to play, in their economies and in the lives of their citizens, over past decades. The more objectives governments try to pursue and to promote, and the more they rely on tax systems to do that, the more complex the tax systems becomes, and the more corruption, tax evasion and high compliance and administrative costs result.

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