

Promoting voluntary tax compliance and accountable public spending

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Can tax administrators affect the “social contract”?

- The promotion of voluntary compliance is a central part of tax administration in most countries, including most developing countries.
- It is plausible that “voluntary compliance depends to a significant extent on people’s perception of the quality and responsiveness of the state. Citizens are more likely to comply with tax laws if they accept the state as legitimate and credible.”
- However, the legitimacy, credibility, quality and responsiveness of a state are largely outside the control of tax administrators and even tax policymakers.

How strong is the connection between effective tax administration and accountable public spending—how likely is there “social contract” in respect of taxation?

- Tax administrators can highlight aspects of effective public spending to boost “tax morale” and increase voluntary compliance. There is at least limited evidence for the utility of this type of public relations campaign.
- Improving taxpayer service is generally regarded as important to securing voluntary compliance, but this is not the same as accountable public spending.
- What, then, is the “social glue” that seems to underlie voluntary compliance?

One possible answer: business firms where investors and workers can earn profit by complying with the law

- Most modern taxes are collected with the assistance of firms: withholding on individual wage and financial income; payroll taxes; VAT and sales taxes; the corporate income tax; environmental taxes and user fees.
- The key to voluntary compliance is thus firm compliance.
- What firms tend to comply more?
 - Larger, more profitable firms
 - Firms the operations of which depend on the provision of public goods, including adequate regulations (e.g. law on labor/employment, workplace safety, environment, food safety, public health, etc.).

The modern firm as the site of social cooperation

- There is evidence that individuals from developed countries show greater disposition to cooperate in game settings, probably due to the fact that they've had more occasions through which to experience cooperation and develop trust.
- Business firms (and workplaces in general) are where most adults experience (i) cooperation regulated/enabled by law, and (ii) the benefit of compliance with the law.
- Thus government regulations that reward compliant firms (i.e. good laws), not public spending per se (e.g. through redistribution), may have a more direct impact on voluntary tax compliance.
- Tax administration itself must (i) follow the rule of law, and (ii) reward compliance.