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Investigating the Simultaneous Impact of Institutional Quality and Tax Evasion on the Performance of the Tax System in Selected Mena Countries

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EXTENDED ABSTRACT

INTRODUCTION

Tax is the main and most stable source of government funding, but governments in most developing countries face institutional and structural barriers, such as poor quality of governance and high levels of corruption, in providing tax revenues. Accordingly, strengthening government accountability and effectiveness can increase the willingness to pay taxes. The trust created in individuals as a result of improving the quality of governance leads to the timely receipt of tax revenues and this leads to strengthening the economic structure. Thus, improvements in institutional quality can lead to public confidence, reduced tax evasion, increased government tax revenues, and ultimately improved tax system performance. One of the important indicators of the tax system performance in different countries is the ratio of tax revenues to GDP in each country. Accordingly, a higher value of this index in a country indicates better performance of its tax system.

METHODOLOGY

In this study, the tax evasion trend is first estimated using Multiple Causes-Multiple Indicators (MIMIC) method. Finally, the simultaneous effect of institutional quality and tax evasion on the performance of the tax system of selected MENA countries in the period (2002-2007) is investigated using the panel data method. In the following, theoretical principles are used to specify the econometric model, in which simultaneous effects of government efficiency and accountability and tax evasion on the performance of the tax system in selected countries of Mena in the period (2017-2002) are discussed:

$$(1)\quad Taxr_{it} = \alpha_i + \beta_1 Ggdp_{it} + \beta_2 Struc_{it} + \beta_3 Sagri_{it} + + \beta_4 \operatorname{Im} p_{it} + \beta_5 Gove_{it} + \beta_6 Tavod_{it} + \varepsilon_{it}$$

Where, $Taxr_{it}$ is the ratio of government tax revenues to GDP, $Ggdp_{it}$ is growth rate of GDP, $Struc_{it}$ is value added ratio of services sector to value added of industry sector (structural conversion index), $Sagri_{it}$ is the share of value added of agricultural sector in GDP, $\text{Im}\, p_{it}$ is the ratio of imports of goods and services To GDP, $Gove_{it}$ is the government efficiency index and $Tavod_{it}$ is the tax evasion index in the i-th country at time t and ε_{it} is the error term. In the second model, the multiplier effects of tax evasion and GDP growth on the ratio of government tax revenues to GDP are examined:

$$(2)\, Taxr_{it} = \alpha_i + \beta_1 Avoid_{it} * Ggdp_{it} + \beta_2 Struc_{it} + \beta_3 Sagri_{it} + + \beta_4 \text{Im}\, p_{it} + \beta_5 Gove_{it} + \varepsilon_{it}$$

FINDINGS

Increasing government efficiency and accountability paves the way for greater public participation in financing government expenditures and increases government tax revenues while reducing tax evasion. Also, increasing trade restrictions expand the underground economy, increase illegal imports and smuggling, and reduce government tax revenues. Also, structural transformation, as a representative of the change in the composition of economic sectors, affects the government's ability to collect taxes, the composition and type of taxes it can impose on the economy.

CONCLUSION

The results show that improving the quality of governance leads to a reduction in tax evasion. Also, the results show that government efficiency and accountability, structural transformation in the economy, the share of imports of goods and services in GDP have a positive effect but the share of value added in agriculture in GDP has a negative effect on the ratio of tax revenues to GDP. In addition, the effect of tax evasion and the multiplier effect of tax evasion and GDP growth rate on the ratio of tax revenues to GDP are not significant.

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