Estimating the Determinants of Tax Morale of India

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1. Introduction

Tax evasion and tax avoidance are challenges often hamper the generation of revenue for the government to function smoothly. In recent years, many empirical studies have focused on tax morale to understand tax non-compliance behaviour better. It is fascinating to know that the individual differences about tax sentiment are not random, hence necessitating careful consideration. Attitudes toward tax obligations are mainly influenced by more than just economic, institutional, and political reasons (Andreoni et al., 1998), such as sense of moral obligation or civic duties (Torgler & Schneider, 2007b). Though many studies have been carried out on this subject; the basic question such as 'why do people pay taxes when they have incentives to evade?' is yet not completely known (Horodnic & Williams, 2019; Yücedogru & Hasseldine, 2016). The popularity of the subject is very recent due to criticisms of economic deterrence models of tax compliance (Yücedogru & Hasseldine, 2016). Various academician has studied tax morale post explanation from Torgler (2007) that tax payment is not only an economic phenomenon and most important taxpayers are not always rational.

Over the decade there are several studies on tax morale covering many developing and developed countries. There are numerous factors affecting tax morale in different ways for each of these countries. To name few individual factors like age, gender, income, education where in the macroeconomic factors such economic development of the country, social security in the country, unemployment rate are few factors that are influential. We in this paper intend to throw some light on factors that are driving forces for India.

We built a simple model with two sets of variables to figure out which factors influence tax morale. The first pertains to people's attitudes on paying taxes based on the demographic factors such as age, education, marital status, religiosity etc. The second category examines the institutional, and economic disparities that exist in the society. These two groups of indicators attempt to capture the individual and contextual sources of subjective heterogeneity in tax morale.

2. Literature Review

The word "tax morale" refers to the complex set of moral and ethical considerations that shape people's attitudes toward paying taxes. As well explained by Luttmer & Singhal (2014) "broadly as an umbrella term capturing nonpecuniary motivations for tax compliance as well as factors that fall outside the standard, expected utility framework". Among the several potential factors that ideally influence tax morale both positively as well as negatively, the literature emphasizes on reciprocity as well as vertical trust. As a holistic approach, many fields specially such as sociology and psychology have contributed factors that can be identified and work favorably for more inclusive society (Prichard et al., 2019). For instance, age, gender, education, marital status, trust in government, trust in public institution, financial satisfaction have positive impact on willingness to pay taxes (Alm & Torgler, 2006; Lago-Peñas & Lago-Peñas, 2010; Torgler, 2004a), whereas self-employed and higher level of income negatively impact tax compliance attitude (Barone & Mocetti, 2011; Martinez-Vazquez & Torgler, 2009).

2.1 Demographic factors:

Even though all group members are exposed to the social norm that paying taxes is right and evading taxes is immoral, their internalization of this standard may vary. Individuals who have tendency to consider morality and ethics as inevitable, foresee this as breach of psychological contract and thus ought to abide by the tax laws (Schnellenbach, 2006). For instance, religious people may believe that there are certain responsibilities must be met no matter what, one of which is paying taxes, because they are concerned with righteousness. Considering genders, women are believed to give regard a higher priority on ethical issues than men; for example, according to Yew et al. (2015) women pay more attention to ethical considerations and are hence more tax compliant than men. According to Grundmann & Graf Lambsdorff (2017), women are more willing to abide tax laws. Similarly, married people tend to show higher tax morale when compared to singles (Capasso et al., 2021; Williams & Horodnic, 2016). Families having children do not support cheating on taxes, i.e. the tax morale is often higher than families with no children (Krasniqi & Williams, 2017).

Elderly people who are believed to have better social ties, and are more inclined to follow tax rules owing to their image, are more likely to believe that tax compliance is a citizen's duty. Lago-Peñas & Lago-Peñas, (2010) found that age and religion positively influence tax morale. Special consideration should be given to the impact of education on tax morale. Preceding empirical evidences such as Torgler & Schneider, (2007) argue that highly educated individuals are conversant about the tax

laws and have fiscal connections. On one hand they are well aware of the benefits they are eligible for on the other, they are critical about the state affairs and their spending on public goods. Thus, it is arduous to clearly predict the relationship of tax morale and education. Martinez & Coelho (2019) found that education is positively connected with tax morale in Brazil. According to Cummings et al. (2009) a comparison between Botswana and South Africa demonstrates that education has no statistically significant impact on tax morale. Thus, religion, gender, age and education should all boost a person's sense of belonging to a society and their willingness to follow the rule that a good citizen should pay taxes. However, we do have chances of finding difference then predicted in the literature for India.

2.2 Economic Variables

Apart from demographic variables it is believed that self-interested citizens form opinions that are influenced by their particular economic circumstances (e.g., employment status, income, financial satisfaction, and income equality). It is presumed that people who are financially sound and benefit from the society conditions are expected to pay more taxes than people who are less privileged. Although capturing the effect of income or the employment status on tax morale might not be easy owning to individuals risk preferences and incidence of taxes (Andreoni et al., 1998). Given this, self-employed individuals are alleged for higher tax evasion as compared to individual working as employees. Thus, opinions on tax morale might reflect an ex-post justification of evading taxes. Empirical evidence reveals mixed results of tax morale among self-employed individuals. Self-employed show negative impact on tax morale (Filippin et al., 2013; Jahnke & Weisser, 2018) while on the other hand there is evidence of self-employed having positive impact on tax morale (Russo, 2013).

3.   Data & Methodology

3.1 Data

To evaluate which among demographic, socio-economic or perceived behavior factors shape tax morale of Indian citizens, we gleaned data from World Value Survey (WVS). The WVS is a global network of social scientists studying changing values and their impact on social and political life, led by an international team of scholars. WVS collects the data from over hundreds of countries capturing the values, beliefs and attitude of citizens (Alm and Torgler 2006; Torgler and Werner 2005; Martinez-Vazquez and Torgler 2009; OECD 2013a; Bilgin 2014). Over the years, WVS has established that people's views do impact economic development.

   The first wave of WVS displays the data collected between 1981-1984, followed by second wave in 1990-1994, and thereafter in 1995-1998, 1999-2004, 2005-2009, 2010-2014 and latest is 2017-2020. India has been part of this survey since second wave, however, the latest wave i.e. wave 7 does not have data from India owing to pandemic. In this study we use pooled cross-section data from all the waves (1990-2010) to understand the changes in the belief, values and attitudes of Indian over changing economic condition of India beginning from liberalisation and in every decade.

   The survey is carried out by professional organizations using face-to-face interviews or phone interviews for remote areas. The WVS aims to assist scientists and policymakers in better understanding changes in people's beliefs, values, and motivations around the world. These data have been utilised by thousands of political scientists, sociologists, social psychologists, anthropologists, and economists to study themes including economic development, democratisation, religion, gender equality, social capital, and subjective well-being. The samples are collected following either full probability or combination of probability and stratified sampling. Minimum sample size of 1200 respondents are collected in each country representing of all people of the country in the age 18 or above.

3.2 Measurement of the dependent variable:

The key dependent variable in this study is tax morale – determining individual's motivation to pay tax. In the survey conducted by WVS, the respondents are asked following question: "Please tell me for each of the following actions whether you think it can always be justified, never be justified, or something in between: cheating on taxes if you have a chance." Responses to this question are collected on ten-scale order where 1 is "never justifiable" and 10 is "always justifiable". We have reconstructed this scale to four-scale order (0,1,2,3) where 3 being highest, covers the responses as "never justifiable" aggregated for two points (1 and 2), 2 combines points 3,4, and 5 as "not justifiable but understandable", 1 stands for 6,7, and 8 as "sometimes justifiable" and lastly 0 is "always justifiable" aggregated for last two points 9 and 10. Considering the original scale of 10 points there is vast difference between the population present in the first category (80%) and second point covers (5%). Due to this steep difference in first and second category, we find it appropriate to reconstruct the code in such a way that data does not loses its variability. Individuals with higher tax morale are the one who believe that cheating on taxes is never justifiable. Contrary to this individual with lower tax morale are the one who do not shy-away from evasion and its consequences, but also justify cheating on taxes.

   Our main specification has following structure

$$TM = \alpha + \beta_1 \, Demo_i + \beta_2 \, Econ_i + \varepsilon \; \dots\dots \; (1)$$

where TM denotes the tax morale. Previous literature emphasizes on considering the relevance of economic variables and socio-capital variables in shaping tax morale. Explanatory variables included in this study are inspired by several studies, like Bilgin (2014), Doerrenberg & Peichl (2013), Rodriguez-Justicia & Theilen (2018), Torgler & Schneider (2007). Our explanatory variables can be classified into three categories: *Demo* constitute of demographic variables; and *Econ* includes economic variables that influence the perception of an individual.

Explanatory Variables:

3.3 Demographic factors.

Demographic variables constitute the information about respondents' age, gender, marital status, education level, religiosity (religious or not) and number of children in the household. Among the demographic variables gender is our main explanatory variable. As extent of literature claims that gender does influence tax morale. In most of the studies females are tend to be more tax compliant than men (Cyan et al., 2016; Doerrenberg & Peichl, 2013; Torgler, 2003). However, in some studies male respondent have shown higher tax compliance than females (Alasfour et al., 2016; Lago-Peñas & Lago-Peñas, 2010). Gender is a dummy variable (1= female and 0 = otherwise). Age is a categorical variable that captures the age of the respondent representing different age groups. Survey targets the respondents who are from working age group that is above 18. Thus, the minimum age is 18 and maximum is 92 years old. We have segregated groups as 18-30 as reference group followed by 31-45, 46-60, 61-75 and finally 76 & above. The literature supports that as the person turns older, the risk aversion increases, hence the expected relationship with tax morale is positive (Bilgin, 2014; Filippin et al., 2013; Lago-Peñas & Lago-Peñas, 2010; Torgler, 2004b). Marital status consists of six categories (Married, living together, divorced, separate, widow, and single). We have reconstructed two categories as (married = married and living together, divorced = divorced and separate) due to less numbers of respondent in individual categories in the respective categories and they have similar characteristics. The number of children is represented as continuous variable. Respondent self-reported themselves as religious, not religious and atheist. Religiosity can impact the willingness to pay taxes positively.

Educational level is yet another interesting variable. We divided it into four major categories as no education, primary education, secondary education and university or above. Education is inevitable factor as it prepares a person with the knowledge necessary to make an informed decision. Since educated people are more aware of government expenditures, other state services, and the allocation of tax revenue, the intuitively expected sign for education level should be positive. Although the effects of education as an independent variable on tax morale are beneficial in Pakistan, Spain and Turkey, it is believed to diminish tax morale in United States and Italy (Barone & Mocetti, 2011; Bilgin, 2014; Cyan et al., 2016; Lago-Peñas & Lago-Peñas, 2010).

3.4 Economic Variables:

Based on the literature we have constructed the variables for employment status as – respondents working full-time, part-time, self-employed, retirees, housewives, students or as unemployed. A part from employment status, income level plays a crucial role in determining the economic status. We derived income level from income scale where respondents were asked to categorise themselves from 1 to 10 scale, where 1 being lowest and 10 being highest level of income. We reconstructed the variable for income based on this scale in three groups, mainly lower income group representing the lower three scales 1 to 3, middle income group representing scale from 4 to 7 and higher income group represents the remaining scale.

3.5 Empirical analysis

In this section we discuss the choice of estimation strategy to identify the determinants of tax morale. To begin, we examined potential determinant of tax morale using an ordered probit model. Since our dependent variable is categorical, we could use either logit or probit model. However, given the choice of method probit models are better in case of random effects and large sample size. Hence, we are using Ordered probit models as our dependent variable has three or more ordered categories. However, because the equation in ordered probit estimation has a non-linear form, only the sign of the coefficient may be immediately evaluated and not its size. Since we are also interested in the magnitude along with the nature, we calculated the marginal effects. Marginal effects are a technique for determining the quantitative impact of a change in scaled dependent variables in our case tax morale (see, e.g., Frey & Stutzer 2002). Thus, in this paper along with the coefficient we also present the marginal effect for the highest value *"cheating on taxes is never justifiable"*. The majority of the outcomes are highly dependable in terms of estimation methodologies.

3.6 Demographic Factors

In table – 1 below we show the estimates of ordered probit model, where the second column exhibits socio-demographic variables with time variants dummy for year 1999 and 2010, keeping 1990 year as reference. Since ordered probit model is non-linear and predicts only the relationship, for magnitude we have calculated marginal effects of higher tax morale. The marginal effects are reported in the same table in third, fifth and sixth columns. To represent the quantitative effects of the variables, we report the marginal effect for the score 3(Cheating is never Justifiable). A female respondent will never justify cheating on taxes when compared to male by 3.05 per cent at the highest level of tax morale. Age and marital status do not show any significant relationship with tax morale. However, the marginal effect for age is growing with the older cohort, though insignificant the results confirm the previous literature that older age people exhibit higher tax morale. Tax morale and education has positive and significant relationship. At highest level of tax morale, a respondent with university and above education is approx. 6.35 per cent more likely to be tax compliant than a respondent with no education. However, literature argues that education has ambiguous result. The same can be seen in our empirical model we can see a differential increase at different level of education when compared to no education. The primary education shows higher tax morale then secondary education respondents. That is primary educated respondent shows 4.95 per cent increase in tax morale compared to no education, where as secondary education shows 3.66 per cent. Since religion draws the implicit rules that bifurcates between right and wrong, religious people believe that certain duties are bound to perform as per the societal norms (Lago-Peñas & Lago-Peñas, 2010).

Following this we find similar results that is as compared to religious people, not religious and atheist people have lower tax morale.

Table 1 *Determinants of Tax Morale*

	I	Marg. Eff TM=3	II	Marg. Eff TM=3
Demographic Variables				
Female	0.1346***	0.0305***	0.2215***	0.0487***
	(0.0374)	(0.0085)	(0.0505)	(0.0111)
31 – 45 Age	0.0422	0.0098	0.0158	0.0036
	(0.0468)	(0.0109)	(0.0503)	(0.0114)
46 – 60 Age	0.0720	0.0164	0.0519	0.0115
	(0.0563)	(0.0128)	(0.0609)	(0.0135)
61 – 75 Age	0.0546	0.0126	0.1524	0.0321
	(0.0719)	(0.0164)	(0.0827)	(0.0168)
76 and above	0.1517	0.0332	0.2261	0.0457
	(0.1577)	(0.0321)	(0.1780)	(0.0321)
Married	-0.0572	-0.0130	-0.0863	-0.0190
	(0.0932)	(0.0211)	(0.0985)	(0.0216)
Divorced	0.0225	0.0051	-0.1138	-0.0250
	(0.2456)	(0.0557)	(0.2616)	(0.0575)
Widow	0.1262	0.0286	0.1341	0.0295
	(0.1374)	(0.0312)	(0.1522)	(0.0334)
Primary	0.2184***	0.0495***	0.2059***	0.0452***
	(0.0548)	(0.0124)	(0.0612)	(0.0134)
Secondary Edu	0.1614**	0.0366**	0.1048	0.0230
	(0.0534)	(0.0121)	(0.0588)	(0.0129)
University & above	0.2801***	0.0635***	0.2706***	0.0594***
	(0.0539)	(0.0122)	(0.0620)	(0.0136)
Not Religious	-0.1455**	-0.0330**	-0.1973***	-0.0433***
	(0.0531)	(0.0120)	(0.0561)	(0.0123)
Atheist	-0.3683**	-0.0835**	-0.4336**	-0.0953**
	(0.1308)	(0.0297)	(0.1323)	(0.0290)
Econ Variables				
Part-time Empl			-0.3582***	-0.0787***
			(0.0766)	(0.0168)
Self-Employed			0.1656**	0.0364**
			(0.0594)	(0.0130)
Retired			-0.2357*	-0.0518*
			(0.1083)	(0.0238)
House Wife			-0.1672**	-0.0367**
			(0.0616)	(0.0135)
Student			-0.1999*	-0.0439*
			(0.0874)	(0.0192)
Unemployed			-0.2898***	-0.0637***
			(0.0782)	(0.0172)
1999-2004	-0.3697***	-0.0839***	-0.3022***	-0.0664***
	(0.0535)	(0.0121)	(0.0645)	(0.0142)
2010-2014	-0.0978*	-0.0222*	-0.0389	-0.0085
	(0.0493)	(0.0112)	(0.0559)	(0.0123)
cut1	-1.8541***		-2.0614***	
	(0.1232)		(0.1382)	
cut2	-1.5682***		-1.7507***	
	(0.1219)		(0.1363)	
cut3	-1.0017***		-1.1393***	
	(0.1207)		(0.1348)	
N	7206	7206	6472	6472

3.7 Economic Variables

All the employment status has significant relationship with tax morale; however, the magnitude differs. When compared to full-time employees; part-time employees, retired, house-wife, students and unemployed show negative relationship, very unlikely to the literature. However, we have opposite results for self-employed respondents compared to various studies carried world-wide. Our study shows that self-employed respondents exhibit positive relation with tax morale. The marginal effects of part-time employed and unemployed is significant at 1 per cent, a one unit increase in part-time employment and unemployment lower the tax morale by 7.87 per cent and 6.37 per cent respectively. A house-wife has lower tax morale by 3.67 per cent at 5 per cent significant level. For Indian diaspora, house-wife are mostly dependent on the male earning member of the family, they most likely are interested in saving each penny to ease their expenditure. Student and retired individual also show negative relationship with tax morale, this is confirming the extent of literature, as students and retired both are in crunch of money and would prefer saving in order to facilitate higher disposable income. It is believed, self-employed is always having more opportunities to evade than an employed individual. Surprisingly, in India, a self-employed are the one honest taxpayer and exhibit higher tax morale by 3.56 per cent as compared to a full-time employed.

4. Discussion

An ordered probit model is used to evaluate the effects of a set of determinants on tax morale in India. According to the distribution of tax morale in our sample, tax morale peaked in 1990, just before tax reform. During the 1990s, the transition to a market economy was chaotic. A thoroughly thought progressive taxation strategy did not succeed in India so far to take into consideration the long-standing informal economy and centrally planned economy (Acharya, 2005). A progressive tax system that was introduced post reforms with revised tax rates, did not brought what it was meant for. Lack of competence in tax administration, tax crimes and policing did not stop and fiscal deficit is still problem for India. Although increase in tax revenue and tax base is evident from recent results but it is not clear if these increase in tax revenue is due to a change in individual intention with respect to tax obligation or is it because of better enforcement act. With this study it is evident that tax compliance is function of both ethics or morale and deterrence factors. Individual's tax decisions are often influenced by the perceptions of others evading taxes or tax administrations behaviour. In India also contextual variables like confidence in government, national pride plays significant role in shaping tax morale. This observations are evident in other international studies as well (Alasfour et al., 2016; Krasniqi & Williams, 2017; Li, 2010; Torgler, 2004b; Yew et al., 2014). Among demographic factors, age, education and religiosity does matter while taking decisions to comply with tax laws. Among economic variables, self-employed shows positive relation with tax morale, this is counter intuitive as self-employed have more chances to cheat on taxes as compared to salaried. Retired shows negative influence on tax morale, the reason could be, in India we do not have social security for elderly hence it is intuitive that these group of people support themselves from pensions. This study provides bases for the policy makers where they can form a policy to increase voluntary compliance by providing social security, transparency in the public institution.

5. References

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