Causes Of Tax Evasion Of The Traders In The Informal Market
Calculation Of The Amount Of Tax Evasion By Means Of The Methodology
Of Real Options

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Abstract

Tax evasion stems from a lack of social consciousness. Similarly, a large number of variables intervene in the decision-making process of an individual or a company when determining whether to pay taxes or not. The purpose of this paper is to prove whether informality arises due to a lack of civic culture among the population of developing nations, particularly in the case of Mexico. Likewise, the methodology used for this investigation takes into account real options as a way to draw a theoretical model from this behaviour. A specific model was selected because it is flexible enough to consider variables related to the country’s economic, political and legal conditions. Additionally, the relative uncertainty of a given individual’s moral standards, education and social consciousness are evaluated through volatility in opinions. In using this methodology, an approximate model of the behavior of a tax evader can be reached and the potential benefits that fiscal authorities could enjoy by studying the conduct of tax evaders.

All data was collected through a survey carried out in a sample of 200 people. Surprisingly, most of the answers provided by the traders express a willingness to step into the formal economy, each taking into consideration his/her specific needs and fiscal capacity. Moreover, the survey’s respondents suggested that a fixed monthly income tax could facilitate their shift. Once an analysis of the obtained data was made, results indicated that tax evasion are due to a lack of information and the absence of trust in government authorities. According to the methodology of real options, a positive effect on taxation as up to $65,000 million Mexican pesos could come from incorporating new taxpayers into the country’s formal economy.

Keywords: Civic culture, Tax evasion, Informal economy, Informality, Real options, Volatility, Tianguis (informal farmer’s markets in Mexico), Analysis in Discrete Time

Introduction

According to Lapinell (2014), a high degree of tax evasion is a significant concern for both developed and developing countries. Federal governments have made important efforts to establish mechanisms to increase the number of taxpayers. Nevertheless, this task is extremely complicated because tax evasion is tied inherently to a country’s informal economy or to illegal activities.

Tax can be defined as an amount of money that must be paid by individuals to the State whenever they are under such an obligation, whether legally or de facto. Furthermore, Lapinell defines the concept of tax evasion as the non-payment of individuals who are obligated to contribute but choose not to while profiting from fraudulent activities, thus resulting in a decrease in the amount of taxes collected.
Fiscal evaders are those who undertake an activity and profit from it, but retain those resources through illegal means which are legally owed to the State.

Given the degree of complexity that tax evasion entails, its dynamic character, as well as the intervention of countless factors that incentivize or promote said situation, Maquino (2014) concludes that an interdisciplinary approach is required to determine the cause and effect of tax evasion.

Likewise, Maquino explains some of the different causes that have been linked to promote tax evasion or increase its effects: 1) lack of tributary consciousness; 2) an opaque tax collection system; 3) an inflexible tax collection system; and 4) a low risk of being detected. It is important to highlight that Tacchi (2013) states that fiscal evasion is impossible to eradicate without adequately adapting to its rhythm. Considering the State’s lack of proactive tax collection, tax evasion occurs as a form of self-defense. Thus, in order for tax evasion to be eradicated, it is important to ensure the presence of a tax authority in order to increase the risk of evasion being detected.

Following this principle, the Tax Administration Service’s (SAT) 2014-2018 Strategic Plan proposes “to strengthen the SAT’s operational strategy by designating skilled personnel to interact with taxpayers, through the use of a preventive approach beginning at the first stages of said taxpayers’ fiscal planning, to strengthen the capacity of timely detection of illegal practices and evasive behaviors, and to have skilled personnel for the detection of elusive practices”. Moreover, it establishes that, “the purpose of the SAT is for fiscal evasions to not remain unpunished and that the sanctions’ general perception is that they will be strictly enforced in accordance with the regulatory powers approved by Congress, thus allowing for more effective, rapid and conclusive procedures of execution”.

**Section name**

The analysis focuses mainly on individuals that are part of the informal economy, more specifically, those who work in farmer’s markets in Mexico. This study has paid special attention to the needs of these traders, for which special surveys were designed to consider, among other things: gender, age, type of product they sell, the sector of the population where they trade (lower class; lower-middle class, middle class, upper-middle class or upper class), if they would agree to pay taxes, and which factor would motivate them most to incorporate themselves into the formal economy. In addition, the study analyzed the level of trust in the government of those surveyed.

To undertake a less rigid analysis and under the assumption that the data acts like a Brownian Geometrical Movement, the quantity of people that work in the informal economy was modeled using a discrete time model. As a result, many calculations were made: daily volatility, crashes in the upswing, crashes in the downswing, trajectory, the neutral risk probability and the option of paying taxes. A daily nodal period was considered for two years.

Once the surveys were processed, multiple scenarios were made in which different variables were modified to analyze their impact. These were volatility, rates of desertion, different ways of taxation and various types of incentives to incorporate new taxpayers to the formal economy.

**Conclusions**

The Federal Government must consider that the aim of incorporating people into the formal economy will not only have a positive effect regarding taxation, it will also have important social, educational, health and security benefits. Of those surveyed, the most important incentive for entering the formal economy is that they will be granted social security and retirement benefits as well as medical services.
Similarly, the study show that civic awareness exists among the general populus. However, mutual confidence between authorities and people is absent. For this reason, it is important to create a payment scheme that adequately takes into account the fact that income is extremely variable for most Mexicans, which ranges from as low as the sale of a piece of candy up to $1,000 Mexican pesos a week.

Thus, while a significant percentage of people are willing to pay taxes, the majority suggests that this payment should be a fixed amount that should be determined according to their level of income. They also suggest that the government should offer workshops about fiscal obligations in order for people to adequately comply to them. As prescribed by the methodology of real options, incorporating new taxpayers to formality will have a positive effect on taxation of up to approximately $65,000 million Mexican pesos.

References


Internet Databases