Inequality shapes the propagation of unethical behaviours: Cheating responses to tax evasion along the income distribution

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Conditional behaviours:

- Cooperation

  Fischbacher *et al.*, 2001; Chaudhuri *et al.*, 2017; Martinangeli, 2021

- Dishonesty

  Gino *et al.*, 2009; Rauhut, 2013;

- Tax evasion

  Frey and Torgler, 2007

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- Do people **react differently according to their own income**?
  - reaction might depend on who they identify with, i.e. "their group" (rich with rich, poor with poor)

Method

- Survey experiment (Italy)
- N = 4000
- Experimental conditions: estimated tax evasion rates at the bottom and top of the income distribution
  (*ad hoc* expert survey)
- Behavioural outcome measure: cheating after die roll Kocher *et al.*, 2018;
- Norm elicitation Krupka and Weber, 2013

Experimental conditions

2x2 information design:

High ev at high incomes High ev at low incomes	Low ev at high incomes High ev at low incomes
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- "Expert survey" among 500 top economists in Italian institutions according to RePEc (2019)

  - Please provide your best estimate of the share of total/capital/labour income that remains undeclared by the following income categories: (list of all quintiles + top decile + top percentile)

  - Construct 4 groups of "experts" according to their estimates: HH, HL, LH, LL

The estimates

Above/below 50% undeclared income for bottom quintile and top decile:

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Above/below 50% undeclared income for bottom quintile and top decile:

Above 50% at high incomes **Above 50%** at low incomes	**Below 50%** at high incomes **Above 50%** at low incomes
Above 50% at high incomes **Below 50%** at low incomes	**Below 50%** at high incomes **Below 50%** at low incomes

Outcome measures

How to measure conditional behaviours in the tax evasion context?

- Cheating
- Norm elicitation

Cheating

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- Notice: The reports are verifiable!

Norm elicitation

- Elicit perceived social norms: Modified Krupka-Weber method on WVS responses in Italy (incentivized)

  In a previous survey study conducted in Italy, a representative sample of the resident population was asked for their opinion about a number of actions. In particular, for each of the following actions they were asked on a scale from 1 to 10 whether they thought it can always be justified (10), never be justified (1), or something in between.
  Your task is to guess which answer was provided most frequently in that survey.

  Claiming undeserved gov.t benefits

  Avoiding a fare on public transport

  Cheating on taxes if given a chance

  Taking a bribe in course of duty

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Hypothesis 1 (Conditional behaviour):

Higher estimated tax evasion induces greater incidence of unethical behaviour.

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- Cheating will increase when we inform people about greater levels of estimated tax malpractice.

Hypothesis 2 (Asymmetric conditional behaviour):

High tax evasion by the rich induces stronger conditional responses than by the poor.

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High tax evasion by the rich induces stronger conditional responses than by the poor.

- Cheating will be higher when estimated tax evasion rates are higher at the top of the income distribution compared to the bottom.

Results

Cheating

VARIABLES	**Probability of misreporting given roll $\neq$ 6**
Baseline: HL	
HH	-0.103**
	(0.052)
LH	-0.082
	(0.057)
LL	-0.068
	(0.087)
Constant	-0.320***
	(0.121)
Controls	✓
Observations	2,843

Robust standard errors,
clustered at region level, in parentheses
*** p<0.01, ** p<0.05, * p<0.1

Cheating

	Probability of misreporting given roll $\neq$ 6	
VARIABLES	Low income	High income
Baseline: HL		
HH	0.043	-0.264***
	(0.106)	(0.078)
LH	0.076	-0.250***
	(0.106)	(0.083)
LL	0.064	-0.192**
	(0.135)	(0.077)
Constant	-0.379***	-0.726***
	(0.138)	(0.148)
Controls	✓	✓
Observations	1,501	1,339

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- But Hypothesis 2 is confirmed for high income respondents.
- **High income respondents cheat more in condition HL compared to any other condition.**
- IV estimation: $pr(Cheating) = f(\hat{post}_r, \hat{post}_p)$
  Only belief updates about tax evasion by high income individuals drive cheating probability among high income respondents

Tax compliance norm

VARIABLES	**Perceived norm of tax compliance**
Baseline: HL	
HH	0.071
	(0.155)
LH	0.369***
	(0.093)
LL	-0.004
	(0.125)
Constant	3.756***
	(0.231)
Controls	✓
Observations	3,421
R-squared	0.020

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Tax compliance norm

	Perceived norm of tax compliance	
VARIABLES	Low income	High income
Baseline: HL		
HH	0.473**	-0.346
	(0.207)	(0.215)
LH	0.510***	0.249
	(0.152)	(0.147)
LL	0.396*	-0.430**
	(0.192)	(0.195)
Constant	3.622***	3.650***
	(0.178)	(0.490)
Controls	✓	✓
Observations	1,787	1,634
R-squared	0.038	0.026

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- The tax compliance norm seems to be determined by how much (little) the poor evade compared to the rich.
- IV estimation: Only belief updates about tax evasion by low income individuals drive norm perception among low income respondents.

Conclusion

- Propensity to cheat increases when tax evasion is presented as more severe among high income than low income individuals
  - Driven by high income respondents

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- Income segments seem to matter:
  - High income more sensitive in a behavioural way
  - Low income more sensitive in their perception of the norm

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