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Gender and Tax Compliance: Firm Level Evidence from Ethiopia

Summary of ICTD Working Paper 113 by Seid Yimam and Fissha Asmare

Many Sub-Saharan African countries, characterised by government budget deficits, have been undergoing reforms and improvements to enhance tax revenue collection. However, such improvements often fall short of expectations and do not yield the expected revenue. These economies are highly vulnerable to tax avoidance and tax evasion, mainly due to the lack of a strong, modernised tax system and limited administrative and enforcement capacity, plus poor awareness of paying tax among the business community.

The Ethiopian government has been implementing activities to boost its tax collection capacity and hence tax revenue. Nonetheless, although the Ethiopian economy has been growing fast, the tax revenue to GDP share has remained low: 13.3 per cent in 2015 and 11.2 per cent in 2019. This is lower than the target of an average of 15 per cent for 2010–2015 and 17.2 per cent for 2016–2020.

An alternative strategy to increase tax compliance and revenue involves harnessing the civicmindedness of individuals, as well as social norms, reciprocity, and cultural values of trust. It is widely suggested that using social enforcement mechanisms to increase tax compliance is more effective than traditional tax enforcement tools like penalty. In Ethiopia, where there is a diversified business community characterised by unique cultural, moral and religious values, it is vital to exploit these social values to mobilise tax collection and improve compliance, presenting tax payment as a prosocial activity. Policymakers therefore need evidence on how social values, norms and individual behavioural differences can play a role in reducing tax evasion; however, no study has yet tried to evaluate the varying effects of such social values on the tax compliance of the business community in Ethiopia. This study investigates the correlation between the gender of business owners and the tax compliance behaviour of enterprises in Ethiopia, addressing the following questions:

- Is there any difference in tax compliance between male and female-owned enterprises?
- Does the gender composition of enterprise owners influence tax compliance?
- Does the impact of the owners' gender on tax compliance vary across firm size?

> "This study explores how tax compliance correlates with key taxpayer characteristics, such as gender."

Data and methods

This is the first study to explore the role of business owners' gender on tax compliance in a developing country context. Its novelty is also in its use of a combination of taxpayers' administrative data and survey data, combining audit registry data from the Ethiopian Ministry of Revenue (MoR) and survey data from 408 enterprises in Addis Ababa. The administrative data contains tax declaration of business income, audit history and penalty information that enables us to determine firms' tax compliant or non-compliant status. Non-compliant businesses are those fined for understating their taxable income at least once between 2008 and 2018. Compliant businesses are those which have never been fined for understating taxable income in that period. Survey data records a firm's characteristics such as the gender of the owners and business environment factors.

> "Improving the participation of women in business may enhance equity and tax revenue collection resulting in better resource mobilisation and development."

Main findings

The findings reveal a statistically significant difference in the tax compliance behaviour of enterprises owned (or majority owned) by men and women, and also finds that the relative gender effect on tax compliance increases with firm size. The results also show that the probability of being tax compliant increases as the ownership share of women in a business increases.

1. Women are more tax compliant than men.
Compared with enterprises owned by men, those owned by women are on average 19.8 percentage points more likely to be tax compliant. This is equivalent to saying that out of 1,000 male-owned businesses with 50 per cent chance of being compliant only 500 will be compliant. However, of the same number of firms owned by women, 700 will be compliant, a far larger number. The result is robust for different gender measurements.

2. Women are compliant not because they fear audit and/or penalty.
Keeping the audit intensity between men and women constant, we find that female-owned businesses representatives strongly disagree with the view that 'people think it is sometimes reasonable to underreport tax' and have a more positive evaluation of the tax system than their male counterparts. Moreover, women are more likely to think it is easier to apply for a tax refund and they also believe the MoR treats businesses more fairly compared to men. All these factors indicate that behavioural variation between genders leads to the differences in the level of tax compliance.

3. Does the effect of gender on tax compliance vary depending on the size of the firm?
The correlation between the owner's gender and tax compliance also becomes stronger as enterprises get larger in size. We measured firm size by its number of permanent employees. The likelihood of being tax compliant becomes higher for women-owned enterprises compared with men-owned ones as firm size increases. For instance, if we compare the marginal effect of gender between firm size 1 and 6, it becomes higher by around 3.4 percentage point for women in the latter case.

Conclusion and policy implications

Based on our findings, we draw the following lessons for policymakers.

- Polices aimed at improving the tax administration system, introducing new tax enforcement and audit practices, and increasing compliance, should consider behavioural differences between male and female business owners.
- The government should emphasise improving women's participation in business, in particular in large companies and semi-private government profitable enterprises. As tax evasion and the tax revenue potential of large enterprises is more substantial than small enterprises, the government can exploit the advantage of women's ethical and tax-compliant behaviour at a larger scale. Finally, this study only explores one aspect of an individual's characteristics – their gender. Further studies should expand on this and examine the role of the untapped diverse social norms, reciprocity, and cultural values of trust existing in Ethiopia for better tax compliance and enhanced tax revenue collection.

Further reading

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Credits

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