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Deterrence and Tax Morale: The moderating effect of corruption in Nigeria

By:

Mpimnee Lucky, Baridoo Friday and Micah Leyira C.

Department of Accounting, Faculty of Management Sciences,
University of Port Harcourt, Choba, Rivers State, Nigeria.

Phone: 234 9054048686; 234 8033542244; 2348034441215

Email; mpimnee@gmail.com; fridaybaridoo@yahoo.com; leyira.micah@uniport.edu.ng

Abstract

This study investigates the influence of deterrent on tax morale; the moderating effect of corruption in Nigeria. The study adopted a quantitative cross-sectional design, population was three hundred and eighty-four (384) individual tax payers across various regions in Nigeria. Data was collected through structured questionnaires administered to participants using Partial Least Squares Structural Equation Modeling (PLS-SEM). Three hypotheses were tested. The results indicate that both deterrence measures; penalties and tax audits have significant and positive effects on tax morale. However, corruption did not significantly moderate the relationship between deterrence and tax morale. This study recommends Nigeria Revenue Service (NRS or the Service) and other relevant tax authorities should strengthen the legal framework for imposing and enforcing tax penalties. Tax authorities in Nigeria should intensify audit efforts and improve audit coverage, especially among high-risk and self-employed taxpayer categories.

Keywords

Deterrence, Tax morale, Penalties, Corruption.

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INTRODUCTION:

Tax morale has been introduced to account for the level of tax evasion. Taxes are important source of revenue however, revenue collection is one of the most important functions performed by any nation and enables it to sustain itself (Smith, 2003; Fjeldstad & Moore, 2009; Anyaduba, Eragbhe & Kennedy, 2012). It is the responsibility of government at different levels (National, State and Local) level to collect taxes. It means that government should not only announce a tax system and wait in hope that taxpayers, through their sense of duty, will voluntarily remit what is owed to the fiscus (Frey, 2003:285; Smith, 2003:1; Slemrod, 2007:25; Croome & Olivier, 2010). Every country has limited economic resources available to meet societal needs.

Tax morale must be put in the general context of the relationship between citizen and the state. At some instances, there are exploitative governments ruling their people in an authoritarian or even dictatorial way. Most governments in history have been of this type, and even today it applies to a large number of nations. Under these conditions, the individuals have to be forced to pay taxes because they know only too well that most of the revenue is not used for expenditures from which they will benefit. In this circumstances the deterrence model is fully applicable.

Many scholars have appreciated that morale is important for explaining tax paying behaviour in a satisfactory way (Torgler 2001). It has been well established that taxpaying behaviour cannot be explained in a satisfactory way without taking tax morale into account.

However, Nobody likes to pay taxes. Government must find a strategy for people to be made to pay their dues. That is, people have to be forced to pay taxes by punishing them if they try to evade such payment. This solution has predominated throughout history. But there are exceptions - in ancient Greece, resources were shifted from the rich to the poor without coercion. Most of the public improvements were built with the liturgy, a voluntary contribution from the rich to the city state (Adams,1993). This solution is also accepted as a matter of course in all countries and for all kinds of taxes which Nigeria is not an exception. Thus, It is assumed that people only pay taxes because the government and its tax administration follow a deterrence policy. This does not mean that one would observe many persons being punished with fines or imprisonment. The idea is rather that the threat of punishment will suffice for people to find it more rational to pay their dues.

The path-breaking contribution by Allingham and Sandmo (1972) on taxpayer behavior is based on the expected utility maximization calculus. It represents a special application of the economic theory of crime championed by Becker (1968). The fundamental insight is that the extent of tax evasion depends negatively on the probability of being caught and the size of the punishment if caught. This model has been extended in various directions. (Andreoni, Erard and Feinstein 1998; Slemrod and Yitzhaki 2002).

Statement of the Problem

While Nigeria depend largely on oil revenue to perform her responsibilities as a government, modern economies depend on tax revenue. It is expected that every taxable citizen pay tax and, in turn, receive public goods and services. But the level of tax compliance is low in Nigeria with the attendant effect of low revenue. This has made the country continually focused on deficit financing during budget. Tax morale is an internalized responsibility or natural motivation to pay tax bills (Braithwaite & Ahmed, 2005). Tax revenue could not be

optimised where citizens evade taxes. It is difficult, if not impossible, to account for the level of tax evasion in Nigeria. Several regulatory policies have been adopted to enhance tax compliance in Nigeria the available records show insignificant improvements. The reason for most tax evasion according to Allingham and Sandmo's (1972) is that taxpayers are rational, risk-averse individuals who are always trying to increase their net income. In view of the low deterrence applied in most countries, taxpayers should evade much more than they actually do. It is widely acknowledged that the decision to evade taxes may not only be driven by factors such as tax rates, penalties, audit probabilities and enforcement but other extrinsic factors.

Despite existing tax provisions aimed at closing loopholes through which taxable individuals or organizations could minimize their tax liabilities, taxpayers continue to employ various avoidance schemes, but it has also led to the neglect of other potential sources of tax revenue. This raises questions about the efficacy of tax officials in their roles. This situation underscores broader issues within Nigeria's tax administration system, encompassing both its design and the attitudes of some taxpayers towards taxation. State governments heavily rely on Pay-As-You-Earn (PAYE) for revenue generation due to its predictability.

This perception of higher penalties and greater difficulty avoiding taxes are both associated with higher tax morale. In Nigeria, Tax morale may also be higher when people believe that payment taxes is with less frequency of corruption among tax officials or the greater the trust they have in tax officials.

This study is determined to find out the influence of deterrence on tax morale and the mediating role of corruption in Nigeria

Theoretical and Empirical Review

The institutional theory

The institutional theory is premised around the idea that organisations seek legitimacy, expectations, rules, and routines (Kuijpers & Eijdenberg, 2021). DiMaggio and Powell (1983) in their seminar work highlighted how organisations try to seek legitimacy by conforming to three forms of institutional pressures that collectively shape organisational behaviours, structures and processes. These institutional pressures include, normative, coercive and mimetic pressures.

DiMaggio and Powell (1983) offers a theoretical framework of “deterrence and tax morale and used institutional theory to showed how organisations and individuals affect taxpayers. This theory posits that organisations do not exist in isolation, rather they are deeply embedded within societal structures which influences their behaviour and practices.

The fiscal exchange theory

The fiscal exchange theory is acclaimed to have evolved from the economic deterrence and the social psychology models (McKerchar and Evans, 2009), and is premised upon the existence of a social, relational or psychological contract between the government and the taxpayers.

Psychological contract theory

Psychological contract theory focuses on the unwritten implicit expectations and obligations that exist between employees and employers beyond formal employment contracts and agreements (Hoglund, 2012).

Deterrence

Deterrent as punishment to tax fraud is an age long tool correcting tax offender and ensuring prompt response to payment of tax levies, as it were from inception tax fraud is astronomically on the increase rather than declining. The seminal reference for analyzing tax evasion decision at the individual level is Allingham and Sandmo (1972) (A&S), who develop a straightforward model of the decision to pay taxes based on Becker's (1968) analysis of criminal behavior. In their model, the level of declared income subject to taxation is decided by weighting the expected costs and benefits of underreporting: on the one hand, the individual can be audited and, if caught, penalized; on the other hand, he might not be audited, and thus escape taxation.

Assuming a given perceived probability of being audited, the individual decides how much to evade so as to maximize his expected utility. In this model it is easy to show that the "optimal" level of tax evasion declines with the probability of being audited, and with the size of the penalty. Above and beyond the quantitative predictions of the model, the A&S framework is the standard theoretical reference in the economic analysis of tax compliance, and it is useful to consider some of its basic constructs in order to gauge its empirical relevance in various contexts; in particular, the opportunities for evasion, the perceived probability of detection and the severity of punishment. What are the opportunities for evasion? From the perspective of the A&S model, what is the realistic empirical counterpart of an individual's taxable income that he or she may have incentives and the ability to under-report? In many cases this is not their total income. In most countries, wages are reported to the tax authority by the employer (often even withholding tax obligations), which makes evasion on such income very difficult. The same happens with income obtained from interest earned on financial assets which are reported to the tax authorities by banks. In these cases, the opportunity for underreporting income and evading taxes is very limited. This suggests that the deterrence model should be interpreted as applying to that part of income (or those categories of earnings) which the tax payer can in fact evade without certainty of detection. Evasion is determined to a large extent by the "opportunity" for income misreporting (Slemrod, 2001). A second issue relates to the perceived probability of being detected or audited. How is this perception determined? The original A&S paper already considers the possibility that this probability is determined endogenously assuming that it declines with the amount of income reported. It is shown that the results derived from the simple model do not change

Finally, the deterrence model not only depends on the probability of detection but also on the severity of the penalty in case an illicit behaviour is revealed. In this regard, public intervention aimed at improving enforcement could increase penalties or increase awareness of existing fines in case of detection.

Tax Penalties

The deterrence measures to crime have been widely discussed especially the extent of how they could be used to reduce crime in the society (Adenuga & Abdulrazak, 2016). The roles of deterrence measures have been noted to increase the monetary cost of public and private

expenditure (Rotimi, Foluso,. Abdul, Saliu, Muiyiwa,2019). They admit that amongst tax enforcement tools are such as tax audits, placement of tax penalties, fine, detainment of assets, subsequent disposal of tax default property and compulsory use of tax clearance certificate for major transitions.

An offence is the violation of any law, regulation and legislation, and any person or persons who is a party to doing any act which amounts to or results in or form part of a serious of facts which together amount to or will result in something which is unlawful is guilty of an offence.

Analysis of the accuracy penalty therefore must include analysis of the corresponding penalties

applicable to those parties. This Part sets out the standards of conduct and the penalties imposed on taxpayers, tax practitioners, and government officials—all within the context of the taxpayer's duty to assess her own tax liability.

Tax Audit

Tax audit is one of the most effective policies to prevent tax evasion behaviour (Slemrod, 2000) and ways to ensure outright compliance. Accordingly, tax audit is relevant to tax administration both developing and developing countries of the world so as to avoid tax fraud (evasion and avoidance) by tax payers such as organization and individuals (Olaoye & Ekundayo,2018).

Modugu nd Anyaduba, (2014)defined audit as a process whereby the tax authority examines certain issues concerning to the profits of a company and its other related returns as it may deem necessary and expedient in accordance with the relevant provisions of the Act. However, the primary purpose of tax audit would be to ascertain the extent to which tax payers may have comply with the relevant statutory provisions of the tax Act in respect of their audited financial statements and other tax related returns. It is usually a routine exercise, which its outcome could lead to a reassessment or referral for special investigation especially if tax evasion is suspected. Therefore, helps to sustain the confidence and integrity reposed in the self-assessment scheme currently in force in Nigeria

Corruption and Tax Morale

The effect of corruption in the public sector on tax morale could simply be explained. Payers pay taxes voluntarily and hope that the tax funds they pay can be used by the government or tax authorities to carry out various development programs to improve taxpayers' quality of life. When the government or tax authority corrupts tax funds, this action disappoints taxpayers and decreases their tax morale. Some previous researches show how the conditions of the public sector (for example, corruption, the legal and tax system) affect the tax morale of the citizens (Bani-Mustafa et al., 2022; Bertinelli, 2020; Nyamapheni & Robinson, 2022; Rosid et al., 2018; Sebele-Mpofu, 2020; Williams & Krasniqi, 2017).

Corruption in public authorities can severely harm tax morale. From a theoretical point of view, corruption can discourage people to comply because of perceived unfairness in the exchange between taxpayers and the state (Feld and Frey, 2007) and induce vertical inequities from additional monetary burdening (Fortin et al., 2007). Rose-Ackerman and Palifka (2016) indicate that bribery distorts the price mechanism and erodes government legitimacy. Torgler (2003) shows that taxpayers are more likely to comply if they feel fairly treated by the government.

The following hypotheses are formulated as follows:

- Ho₁: Penalties does not significantly drive tax morale in Nigeria.
- Ho₂: Tax audit has no significant effect on tax morale in Nigeria.
- Ho₃: Corruption has no moderating influence on the relationship between deterrence and tax morale in Nigeria.

Methodology

The study adopted a quantitative cross sectional research design. The study's population under consideration was three hundred and eighty-four (384) individual tax payers across various regions in Nigeria. The accessible population was limited to all self-assessed individual taxpayers, tax consultants and tax professionals, staff of both federal and state inland revenue services in Nigeria. The technique used for collecting the data was a self-developed questionnaire, containing items of diverse formats: multiple choice measured on the 5-point Likert scale, and open-ended questions.

Respondents were chosen through the quota sampling method with regards to specific level of education, that is, those having at least secondary qualification. Moreover, sampling frame was divided into non-overlapping strata for example ethnicity, age, gender and employment.

In line with the objective of the study, the primary data collected was analysed using the statistical package for social sciences (SPSS Version 25) and the Smart PLS V

The SPSS was used for analysing the descriptive statistics and the preliminary analysis of the study, while Smart PLS was employed for the inferential statistics and testing the research hypotheses.

In carrying out the reliability of the research instrument, the Cronbach's Alpha was used. Cronbach's alpha (α) is an estimate of reliability, specifically the internal consistency, of a test or scale. Cronbach's alpha seeks to measure how closely test items are related to one another and thus measuring the same construct.

Model Specification

Following the review of related literature by various scholars and authors on the subject matter, Deterrence and Tax morale in Nigeria, the researcher deem it necessary to express the relationship that exist between these variables in a mathematical model.

$$TMO=f(PEN,TAD/ COR)$$

Expressing equation in the econometric form of the model for the study are given below:

$$TMO_i = \beta_0 + \beta_1PEN_i + \beta_2TAD_i + \beta_3COR_i + \mu_i$$

Where:

$$TMO = \text{Tax morale}$$

;

$$PEN = \text{Penalties}$$

$$TAD = \text{Tax audit}$$

$$COR = \text{Corruption}$$

$\alpha_0, \beta_0, \phi_0$ = regression constant

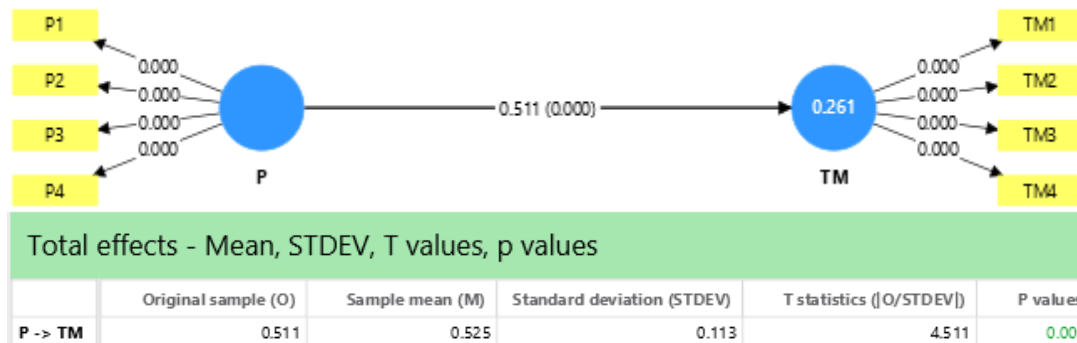
μ = stochastic error term.

Result and Discussions

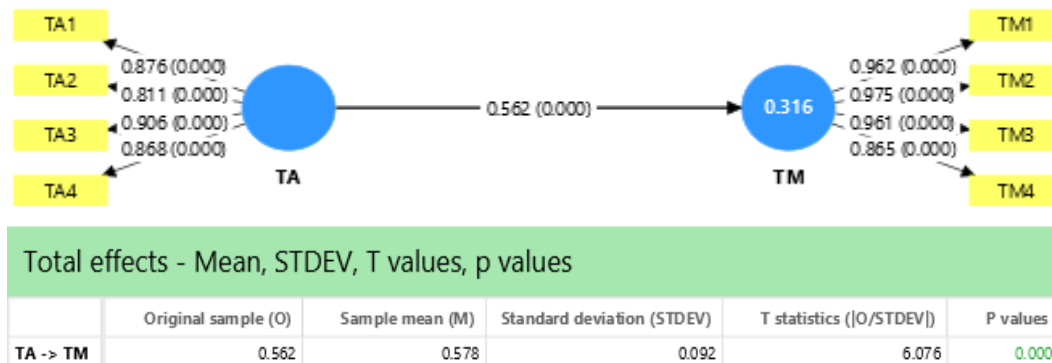
Test of Hypotheses

Hypothesis One

Ho₁: Penalties does not significantly drive tax morale in Nigeria.



Ho₂: Tax audit has no significant effect on tax morale in Nigeria.



Hypothesis 1 (*Total effect*)

The analysis of the relationship between penalties (P) and tax morale (TM) reveals a statistically significant positive effect. The path coefficient (0.511) suggests that increased penalties are moderately to strongly associated with higher levels of tax morale among taxpayers in Nigeria. This means that when individuals perceive penalties for tax evasion to be more severe, certain, or swift, their intrinsic motivation to comply with tax obligations tends to increase. The bootstrapped sample mean (0.525) closely mirrors the original coefficient, indicating the result is stable and consistent across resampling iterations.

Furthermore, the t-statistic value of 4.511 far exceeds the 1.96 threshold for significance at the 5% level, and the p-value of 0.000 confirms that the relationship is not due to chance. Based on these findings, the null hypothesis (Ho₁), which posits that penalties do not significantly drive tax morale in Nigeria, is rejected. Therefore, penalties are indeed a significant predictor of tax morale in the Nigerian context.

This finding aligns with the assumptions of deterrence theory, which suggests that individuals are more likely to comply with laws, including tax laws, when they perceive a high likelihood

of detection and punishment. In Nigeria's context, where tax evasion remains a concern, the enforcement of tax-related penalties can serve not only as a deterrent but also as a mechanism that reinforces the moral obligation to pay taxes. It emphasizes that beyond mere fear of punishment, a structured and consistent enforcement framework can enhance citizens' belief in the fairness and necessity of contributing to the state through taxes.

Hypothesis 2 (*total effect*)

The statistical result for the relationship between tax audit (TA) and tax morale (TM) demonstrates a significant and positive association. The path coefficient of 0.562 indicates a strong positive effect, suggesting that increased audit activity corresponds with higher levels of tax morale among Nigerian taxpayers. In other words, the more likely individuals are to be audited, the greater their internal motivation to comply with tax laws. This is further supported by the bootstrapped sample mean (0.578), which closely aligns with the original estimate, reinforcing the consistency of the relationship.

The standard deviation of the path coefficient is relatively low (0.092), which means there is minimal variability in the bootstrapped estimates. More importantly, the t-statistic value of 6.076 is substantially higher than the critical threshold of 1.96 required for significance at the 5% level, and the p-value of 0.000 confirms that this effect is highly statistically significant.

Based on these results, Hypothesis Two (H_{02}) is rejected, establishing that tax audits do indeed have a significant effect on tax morale in Nigeria.

This finding aligns with the broader framework of deterrence-based tax compliance models, which argue that the likelihood of being audited serves not only as a deterrent to tax evasion but also reinforces a sense of accountability and compliance among taxpayers. In the Nigerian context, where enforcement mechanisms may often be perceived as weak or selectively applied, a visible and fair auditing process may contribute significantly to improving the psychological and moral motivation to pay taxes. Thus, this result underscores the importance of strengthening audit systems as a strategic tool to enhance voluntary tax compliance and public trust in the tax system.

Ho3 Corruption has no moderating influence on the relationship between deterrence and tax morale in Nigeria.

The analysis examining corruption as a moderating variable in the relationship between both deterrence and tax morale, reveals statistically insignificant effects. Specifically, the interaction term for corruption \times deterrence ($C \times \text{Deterrence} \rightarrow \text{TM}$) yields a path coefficient of 0.003, with a very low t-statistic (0.018) and a p-value of 0.985, indicating no significant moderating effect.

This result suggests that, contrary to expectations, the perceived level of corruption in Nigeria does not meaningfully alter how penalties, audits, affect taxpayers' intrinsic willingness to comply with tax obligations. One possible interpretation is that corruption in the public sector may be so normalized or disconnected from personal tax behavior that it fails to dampen or amplify the effects of deterrence. Alternatively, it may reflect citizens' resignation to

systemic corruption, thus weakening its potential to interfere with their tax-related attitudes, whether motivated by fear of enforcement or religious teachings.

While this outcome may appear counter intuitive, it highlights the complexity of corruption's influence and suggests that its moderating role may depend on more nuanced factors such as perceived fairness, trust in institutions, or individual ethical thresholds. Future research may benefit from exploring perceived corruption intensity or sector-specific corruption to better understand its interaction with tax morale determinants.

Conclusion

Based on the finding, we concluded that both penalties and tax audits significantly enhance tax morale, underscoring the importance of enforcement in deterring non-compliance

The study concludes that external enforcement (deterrence) play complementary roles in promoting tax compliance in Nigeria.

Finally, the study concludes that there is no significant moderating effect of corruption on the relationship between deterrence and tax morale and must be addressed through broader institutional reforms, transparency, and trust-building measures in public governance.

Recommendations

The following recommendations are made from the study. They include:

Given that penalties significantly influence tax morale, the government through the Nigeria Revenue Service (NRS or the Service) and other relevant tax authorities should strengthen the legal framework for imposing and enforcing tax penalties. This recommendation is captured in the Nigeria Tax Act, 2025. In the Act, there is a significant increase in non-compliance penalties and the introduction of new penalties. Some of the updates include increase in the penalty for failure to file returns to NGN100,000 in the first month, and NGN50,000 for every month the failure continues, introduction of new penalties such as penalty of NGN5million for awarding contracts to individuals or entities that are not registered for tax, penalties for failure to grant access for deployment of technology, inducing a tax officer etc

Tax authorities in Nigeria should intensify audit efforts and improve audit coverage, especially among high-risk and self-employed taxpayer categories.

The government should prioritize anti-corruption reforms in tax administration by promoting transparency, digitizing tax processes, ensuring accountability of tax officers, and prosecuting corrupt officials.

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