

Tax Avoidance and Tax Evasion in Bangladesh: Methods, Causes, Consequences and Remedies

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Abstract:

In Bangladesh, the concept of 'Tax' is as familiar as 'Tax Avoidance' and 'Tax Evasion'. Developing and unindustrialized countries like Bangladesh are the nastiest victims of tax avoidance and evasion. Along with a very poor tax culture and low compliance rate, Bangladesh has a very robust informal economy. The development activities are hampered in Bangladesh because of low revenue collection, which is the outcome of high tendency of tax evasion and avoidance by the individual taxpayers and corporations of the country. The government must discover the aims behind tax avoidance and evasion of taxpayers, investigate the loopholes in country's tax laws and should take more preemptive measures for developing a strong economic infrastructure. The purpose of the present paper is to discuss the methods, causes, consequences and remedies of tax avoidance and evasion in Bangladesh.

Keywords: *Tax avoidance, Tax evasion, Taxpayers, NBR.*

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I. Introduction

In Bangladesh tax avoidance and tax evasion is a prodigious problem. Both these occurrences are possibly as old as taxation itself. Many individual taxpayers and corporations evade and avoid tax in our country. Tax avoidance and tax evasion are many times considered as similar thing. But both these thoughts are completely different. Tax avoidance can be said as tax minimization by efficient tax planning. Whereas cover-up or concealment of taxable object or failure to pay tax in time either by the taxpayers or their agents is called tax evasion. This paper focuses on the methods, causes, consequences and remedies of tax avoidance and tax evasion which will be supportive in future.

II. Literature Review

Both these phenomena of tax avoidance and evasion are demarcated by several researchers in various ways. Although both result in loss of government revenue, tax avoidance is legal but tax evasion is illegal. Khan et al. (2000) has presented that a huge number of corruption by tax officials is a serious problem for the tax administration in countries like Bangladesh. Bobek and Hatfield (2003) said that, ethical beliefs of individuals can be the best means for enlightening tax obedience. Rahman (2005) indicated that, a noteworthy amount of revenue losses in Bangladesh for tax evasion. Kaibel and Nwokah (2009) have found that, a common problem is faced by every tax system is tax avoidance and evasion. In a study, Green (2009) has identified, why tax evasion should be treated as morally wrong, arises questions. Buehn and Schneider (2012) said that, in the year of 2007, the average size of the shadow economy comprised of 37.4 percent of the GDP in developing countries. According to Oxfam (2013), tax evasion broadens the circle of poverty and erodes the economy of developing countries. Hasan (2014) has specified that, a solid ethical conviction will motivate more people in becoming an exemplary taxpayer.

From the above view of literature I have found that, maximum researchers focus only on tax evasion. There is an enormous gap in previous studies about the causes and methods of both tax avoidance and tax evasion. Tax avoidance is taking advantages of tax laws and loopholes to minimize tax liability in legal ways. Although, tax avoidance is legal but it causes a huge loss of government revenue thus undesirable. So, in my opinion, taking preventive measures only for tax evasion is not enough to solve this vigorous problem. This article has focused on the modes, causes and consequences of both tax avoidance and evasion in Bangladesh and has suggested some protective remedies which can play significant role in future.

III. Objectives of the study

The major objective of the study is to find out the methods, causes, consequences and remedies of tax avoidance and tax evasion in Bangladesh.

The specific objectives of the study are:

1. To discover some obvious means and motives of tax avoidance and tax evasion used by taxpayers in Bangladesh.
2. To analyze significances of tax avoidance and tax evasion in the economy of Bangladesh and suggest some medications to overcome this problem.

IV. Methodology of the study

Descriptive research method is used to attain the objectives. The study is based on secondary data. Secondary data was collected from various newspapers, magazines and books. Additionally, different working papers, journals, articles and websites have been pursued enriching the literature of the study. MS word has been used for summarizing and elucidating the collected data thoroughly. As the study is conceptual in nature so no survey was made for gathering primary data and no financial data are analyzed here.

V. Methods of Tax Avoidance

Tax avoidance is done legally by effective tax planning. Some common methods used by taxpayers to avoid tax are given below:

1. Under pricing is used for reduced tax base to avoid a value added tax. To avoid specific duty, predominant misstatement of measure is often used.
2. The dissimilarity between “professional expenditures” and “personal expenditures” is a worry for taxpayers and tax authorities. Any terms of tax law which is a vague cloudiness is a prospective source of tax avoidance.
3. Forming distinct legal entity such as trust or foundation is an additional tactic to avoid tax. Assets are transferred or donate for the welfare of the foundation from one’s property so that gains may be released or income earned, within this authorized entity rather than earned by the original proprietor, back to the inventor of the trust but not as individual.
4. To minimize tax liability Multinational Companies (MNCs) manipulate price of physical products and also falsify prices of intangible assets such as intellectual property rights (IPR), management services and insurance.
5. Individual taxpayers transfer their property in the name of wife or dependent child to reduce the level of income and tax liability.
6. By creation of Private Limited Companies with the family members, friends and relatives, the management shows expenses and allowances in that way which helps to lessen tax liability.
7. Any business concern or company can avoid tax by transferring a proportion of profit prior to the declaration of dividend to capital reserve or converting it to capital.

However, beside these common methods of tax avoidance an individual can minimize his/her tax liability by cunning tax planning e.g. investment on tax free government securities, investment on residential house, investment on savings instruments, investment on life insurance premium, group insurance premium etc.

VI. Methods of Tax Evasion

Pursuing illegal means to cut or eliminate tax charge is called tax evasion. Typically, this includes either knowingly under-reporting earnings, or deteriorating to show any income at all. Tax evasion may be defined either as the underestimate or suppression of taxable item or as the failure to pay tax in time either by the taxpayers or his/her agent. So, it is illegal. Some common methods used for Tax evasion are discussed below:

1. Importation or exportation of illegal products by using unauthorized approach is one of the common methods of Tax evasion. A trafficker escape customs duty since the products is not moved through an official or notified customer’s port. So they easily not declare the payment of duties and taxes.
2. VAT (Value Added Tax) is basically an indirect tax, which is an extended form of turnover or sales tax. The consumer who ultimately bears the tax burden has minimum scope to evade tax but the producers or distributors who collect VAT from the consumers has chance to evade tax by under reporting the amount of sale.
3. By under invoicing and misstatement of quantity and product description, the importers resist dodging customs duty.
4. Single taxpayers may escape tax by not revealing their other sources of income, same as a business may conceal income by not combining their branch income properly.
5. Many corporate businesses maintain duplicate records of their economic activities to evade tax.

VII. Causes of Tax Avoidance and Tax Evasion in Bangladesh

Responsibility of tax avoidance and evasion in Bangladesh does not rest on any single factor. Akram et al (2012) said that, “motivated by many factors, that grounds of tax evasion in Bangladesh are compound”. Some vital motives for tax avoidance and tax evasion are:

1. In developing countries like Bangladesh, corruption by tax officials is a major problem for the tax administration. In return for illegal indulgence or bribe, corrupted tax officials abstain from reporting when they identify an occurrence of evasion. Increase in corruption and reduction of income tax moves parallel.
2. High tax percentage can be considered as one of the main motives of tax avoidance and evasion in Bangladesh. Compared to other countries, corporate tax rate is high in Bangladesh. High tax rate adversely affect savings and capital formation.
3. Maximum taxpayers have less knowledge about tax law and get minimum information from the tax department. In Bangladesh, lack of knowledge regarding tax laws is another cause of tax evasion.
4. The tax authority in Bangladesh depends on the taxpayers to get information about their income and financial transactions. These loopholes make taxpayers able to hide or twist the affairs which will state true information about their income.
5. Tax administrations of developing countries are commonly inefficient and ineffective. Inefficiencies of tax officers and difficult regulations lead the taxpayers towards tax evasion and avoidance.
6. Bangladesh has a very complex tax law. A complex tax structure demotivates honest taxpayers to calculate actual payable tax amount and encourage dishonest taxpayers to find ways to avoid or evade tax. The present tax structure of Bangladesh is multifarious and full of rebates and exemptions. The complexity occurs because of repeated changes in tax laws which boost the tendency of taxpayers towards tax avoidance and tax evasion.
7. Bangladesh has lacking of preventive measures for tax avoidance and tax evasion. In addition, corrupted tax officers help the taxpayers to avoid or evade tax by using different means in exchange of speed money.
8. Political intentions of the government and tax evasion are closely related with each other. Politicians stab to control the tax administration to obtain political gain. To earn political support from the influential and wealthy members of the society, the government of Bangladesh often influences tax policies. One of the provisions of law in Bangladesh is that, politicians could receive gift from relatives without paying tax which has allowed black money holders to evade tax and legalize their black money.
9. As taxpayers have to pay tax directly from their income, they consider it more as liability than public duty. So, this is a general tendency of taxpayers to find out the tax rebates and exemptions to lead their tax liability as minimum as possible.

Along with these discussed reasons, there are some other aims behind tax avoidance and tax evasion. These are: failure of government for providing basic public goods and services, lack of transparency and accountability in the use of public funds, high costs of gather necessary information and paying tax etc.

VIII. Consequences of Tax Avoidance and Tax Evasion in the Economy of Bangladesh

Even though the core objective of tax avoidance and tax evasion is same, but there is some dissimilarity on their application. Tax evasion is illegal because here, tax liability is reduced by using illegal means or tax is paid not at all. On the other hand, tax avoidance is legal, because in this case, tax liability is minimized by taking the advantages of tax rebates and exemptions and by making proper tax planning. However, tax avoidance or evasion both has a negative impact on the economy of country. Developing countries like Bangladesh, where more than 80% of government revenue is collected from tax, the socio-economic impacts and consequences of tax avoidance and evasion are very severe. Some of the consequences are discussed below:

1. Government revenue reduction or loss is the ultimate result of tax avoidance and tax evasion. It causes falls of improvement expenses and affects the treasure distribution function of a country.
2. NBR estimated that, gigantic revenue is lost each year because of tax avoidance and tax evasion in Bangladesh. With the increase of tax evasion, the size of informal economy also increases.
3. To evade tax, taxpayers also transfer illegally earned money to abroad which make the country's economy weak.
4. Tax laws become distorted because of tax evasion and tax avoidance. In developing countries like Bangladesh, tax laws are edited by tax authorities to counter the activities commenced by wealthy individuals and large corporations to avoid and evade tax. Tax authorities need to change tax laws to prevent measures taken by the taxpayers and tax advisers.
5. Price of luxurious goods rises as taxpayers used their tax evaded income for consuming such goods. As a result, honest taxpayers get frustrated as they find themselves priced out of the market and get inspired to avoid and evade tax.

6. The proficiency and fairness of tax administration is doubted because of high tax evasion and avoidance as tax burden falls to the low income taxpayers. If there is tax evasion, tax administration is considered biased and loses their creditability.
7. For the development of the economic condition of a country, investment by the government can play a vital role. But investment will need fund. Barriers for such investment are created by this unethical practice of avoiding and evading tax.
8. With the loss of government revenue for tax evasion and avoidance, it is becoming harder to ensure income and wealth re-distribution by the government. As a result, the fundamental goal of gathering tax is remaining incomplete.

Alongside, increase of administrative cost, failing to achieve tax and policy goals, reduction of revenue and badly affected social equity, Unemployment problem, less investment in industry are some other consequences of tax avoidance and evasion in Bangladesh.

IX. Remedial Measures to Prevent Tax Avoidance and Tax Evasion

As tax avoidance and tax evasion are one of the key problems for developing the economic condition of Bangladesh, the government and the tax authorities must take some anticipatory actions to control these vicious cycles. Some of the counteractive events are conferred below:

1. Nothing can mislead the taxpayers if they are aware of the significance of paying tax. So, awareness of taxpayers may be developed by arranging public seminars, campaigns etc.
2. The NBR needs to make taxpayers knowledgeable about tax file return, calculation of tax liability accurately and the penalties involved in tax evasion. More the people get knowledge, less the tendency to evade tax.
3. The taxpayers do not want harassment while submitting the tax file and paying tax. Income tax fair may help the taxpayers to return their file and pay their tax easily without any annoyance. Income tax fair is a new concept in Bangladesh and the reaction of taxpayers is positive regarding this concept.
4. A simple reward can motivate a lot. Highest taxpayer or regular taxpayers may be rewarded by the NBR for fulfilling the public obligation properly, which may motivate others.
5. The provision of penalty should be stricter not only for the evaded taxpayer but also for the dishonest tax officials who helps them to evade tax. Relating with the amount of evaded tax, the rate of penalty should be progressively higher.
6. Tax rate can be minimized to control tax avoidance, as high tax rate leads to low savings and less capital formation.
7. To control corruption among tax officials, tax administration could be reformed and the level of punishment should be increased for corrupted officials.
8. The rules regarding tax rebates and exemptions could be restructured and could be more concise to control tax avoidance.
9. The tax rules of Bangladesh are more complex and ambiguous, which makes taxpayers confused and lead them to evade tax. Tax rules should be presented as simply as possible to the taxpayers for their better understanding.
10. The low coverage of the entire income tax is attributed because of the failure in order to bring the persons who legally liable under the enclosed procedure of tax system. Tax revenue could be maximized by the wide base and a low rate structure.
11. Bangladesh's pitiable income tax compliance indicate the country's insufficient tax culture which needs to be improved urgently to combat the evils of tax evasion in Bangladesh and to overcome the poor tax culture.
12. The government of Bangladesh should voice its concern in the international arena to make the MNC's accountable and more transparent in their accounting disclosure. A global standard should be developed under which, all the MNCs will declare about their earning profit and their paying tax amount which will help to control tax evasion and avoidance.

Along with applying of many preventive measures, a Central Intelligence Cell (CIC) has also established as a part of NBR. The CIC performs as tax intelligence function and investigates tax evasion and fraud cases in the areas of income tax, customs and value added tax. However, despite of taking many initiatives still tax avoidance and tax evasion is very high in Bangladesh.

X. Conclusion

Government is legitimately liable to serve the public and to ensure their basic rights. But any development needs fund and in Bangladesh more than 80% of government revenues come from tax. The malicious cycle of tax avoidance and evasion is not only a huge barrier for economic development but also responsible for social discrimination. In every financial year, government prepare budget for the development of

the country, based on their estimated earning revenue from tax and other sources, which remains fragmentary for the reason of high amount of tax avoidance and tax evasion. Every year, a gap between budgeted revenue and collected revenue is a huge threat for our economy which obliges the government to borrow loan thus the economic development is affected badly. To prevent this vicious cycle of tax avoidance and tax evasion, 'tax morale' need to be developed until it is too late to recover. Government must be more aware regarding this problem and make more strict laws and penalties for the tax evaded taxpayers and corrupted tax officials. When the entire citizen will fulfill their obligations towards the country and pay tax properly on time and will support the government to build an economically strong nation, only then a country like Bangladesh can move forward from developing to developed country.

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