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Tax Morale in the Republic of North Macedonia: Analysis of Tax Morale Determinants



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Center for Economic Analyses



**Tax Responsibility Project – Towards Civic
Responsibility and Responsible Tax**



Tax Morale in the Republic of North Macedonia:

Analysis of Tax Morale Determinants

CENTER FOR ECONOMIC ANALYSES (CEA)

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Introduction

An increase in fiscal revenues requires an effective and efficient tax system, measures better tax compliance and tax morale, as well as better training and capacity building of the tax administration.

There is field-based evidence from the experiments conducted by the World Bank, related to the social, psychological, and economic factors that affect taxpayers in making their decision on whether or not to pay taxes. Studies for certain countries have demonstrated that specific messages which the tax offices send to taxpayers, such as communication with the target taxpayers with the purpose of influencing their decisions, may prove to be a fast and low-budget solution for an increased rate of tax collection.

Interventions in the tax system, which also take into consideration human behavior, help individuals/taxpayers to better process the information, to submit their tax returns within the deadline, as well as to help public revenue office staff to better perform their operations. This approach entails the social, psychological, and economic factors, which affect the taxpayers in the decision-making for tax payment. The approach also focuses on tax administration, types of technologies used and services delivered, which are often being neglected when designing standard tax policies. It can all hugely impact the effectiveness of the programs and projects for improving revenue collection, particularly in countries with relatively low collection rates. This approach can provide creative low-budget implementation solutions for some serious challenges¹.

¹ Behavioral Insights for Tax Compliance <http://documents.worldbank.org/curated/en/472181576511865338/pdf>

Methodology

The approach and the methodology used for this analysis were comprised of gathering and analyzing 1) secondary and 2) primary data, as well as office-based research and field surveys.

Office-based research was conducted by using research literature about behaviorist approach to tax policies and its implications on the tax morale. An overview of the legal framework of the country's tax system was conducted, as well.

The field research was conducted by a specialized research organization Indago. The design of the methodology for a qualitative field research was carried out on a representative sample – by interviewing a small portion of a heterogeneous population. A multi-step random sample was used by selecting sampling units based on the probability which is proportionate to the size of the population. The number of primary sampling units (PSU-Primary Sampling Units) in every stratum is proportionate to the size of the assessed population in the respective stratum. The data from the last 2002 census, as well as the latest 2017 population assessment, both served as the basis for assessing the population size.

All eight statistical planning regions were taken for the study (NUTS 3): Skopje, Vardar, Eastern, Southeast, Pelagonia, Southwest, Polog and Northeast region. Every region has furthermore been stratified based on the level of urbanization, i.e. based on the urban and rural strata. From a total of 16 strata, the number of primary sampling units (primary sampling units - PSU) into every stratum (regions and urban/rural level) is proportionate to the size of the assessed strata population. The primary sampling units are often minor units of a geographical area within the stratum. For this particular study, the constituencies were used as primary sampling units, with a sample size of 1000 respondents.

The respondents who participated in the study were grouped based on the regional offices of the Public Revenue Office (RO Skopje, RO Tetovo, RO Bitola, RO Prilep, RO Shtip, and RO Strumica).

1. The Concept of Tax Morale

Taxation as a topic has always been debatable and there have always been diverging opinions about the philosophy behind taxes and taxation in general. Other questions that arise from this topic are who is to pay taxes and at what rates? Is it more essential to collect or to redistribute revenues? Are taxes collected just to correct the deficiencies of the market operations and/or to change the behavior of the economic agents? Is there a fair amount or a fare rate of a specific tax? Are taxes considered only as a legal liability or a morale dimension, as well?

The following categories have to be taken into consideration when adopting a solid tax policy: equality and fairness, safety, effective tax administration, data safety, tax neutrality, economic growth and efficiency, transparency and visibility, minimum tax gap, and accountability to the taxpayers and the rule of law.

However, there is another aspect that needs to be taken into consideration, and that is tax responsibility and tax morale.

Tax morale is defined as voluntary compliance with tax laws and the creation of a social norm of responsibility for paying taxes. *“The tax morale measures the perception and the attitudes of taxpayers for paying or avoiding taxes.”* (OECD 2013)². In its principles of good tax administration, the OECD underlines the importance of tax morale by stressing that “promotion of voluntary compliance with the laws has to be a major concern of the tax authorities”. Improving tax morale is one of the aspects that the tax administration has to consider, in addition to the primary concern for collecting tax revenues.

Tax compliance³ refers to the voluntary comprehensive compliance with all tax laws. That means that the tax returns have to be submitted within the deadline, that the revenues have to be accurately listed and that payment of assessed taxes has to be made by the due date⁴. In addition to including tax compliance, tax responsibility is a wider concept that includes the moral dimension and the responsibility for the entire society in a given institutional context (approach by taxpayers). On the other hand, the responsible tax payment approach aims at tax systems that are open, taxes that can develop and it takes into consideration the interests of all the stakeholders – the governments, the taxpayers and the communities (an approach that takes into consideration the tax rights). The topic of responsible taxes opens up the moral dimension of taxation, as well as its interpretation, the application and implementation of tax procedures.

There are several theories and models of studying the concepts of tax morale and tax evasion, one of them being the theory of unexpected benefit with the idea that in a risky and uncertain situation of being caught and sanctioned for tax non-compliance,

² OECD — State building and Accountability —Tax morale <http://www.oecd.org/tax/tax-global/work-on-statebuilding-accountability-effective-capacity-development.htm>

³ Note: the term tax-compliance will be used for voluntary tax payment in line with the laws

⁴ Water Integrity Network — Tax compliance <https://www.waterintegritynetwork.net/2015/12/04/tax-compliance/>

individuals happen to behave contrary to the assumptions of the model of expected benefit. Hashimzade (2012⁵) claims that the probability of tax control is not obvious when it comes to an average taxpayer. According to the model of economy of crime (Becker, 1968) and (Allingham and Sandmo, 1972⁶), the decision of an individual to evade taxes, on one hand, depends on the probability of being discovered, while on the other hand and it depends on the tax evasion sanctions. In other words, the decision about evading taxes depends on the implementation, and introducing stricter tax controls and/or more severe sanctions would help reduce tax evasion. However, the empirical support for this model is controversial. The debate on this topic becomes more complex by adding the category of tax morale and culture (Lewis, A., Carrera, S., Cullis, J., & Jones, P. (2009)⁷. In the early 90s, there were theories based on social norms (Alm, McClelland, & Schulze, 1992a, 1992b), as well as on ethical aspects of tax evasion (McGee, 1994)⁸.

The tax culture of a certain country derives from the interaction of the stakeholders and the moral values, such as honesty, justice and the feeling of obligation. (Nerre, 2008⁹). Therefore, taking into consideration the values and the norms in a social and demographic context can provide a better explanation as to why people decide to comply with the tax regulations. The term “*tax morale*” is defined as a moral obligation and a belief in a better society by paying taxes. (Frey and Torgler, 2007¹⁰). Tax morale measures individual attitudes towards paying taxes, unlike tax evasion, which measures individuals’ behavior.

Based on the approach which Doerrenberg (2010¹¹) has used, determinants which impact the tax morale, such as demographic factors, are divided into socio-demographic factors/variables and socioeconomic variables, both being illustrated in the following table.

⁵ Hashimzade, N., Myles, G. D., & Tran-Nam, B. (2012). Applications of behavioural economics to tax evasion. *Journal of Economic Surveys*

⁶ Allingham, M., & Sandmo, A. (1972). Income tax evasion: A theoretical analysis. *Journal of Public Economics*, 1(3), 323-338.

⁷ Lewis, A., Carrera, S., Cullis, J., & Jones, P. (2009). Individual, cognitive and cultural differences in tax compliance: UK and Italy compared. *Journal of Economic Psychology*, 30(3), 431-445.

⁸ McGee, R., & Benk, S. (2011). The ethics of tax evasion: A study of Turkish opinion. *Journal of Balkan and Near Eastern Studies*, 13(2), 249-262

⁹ Birger Nerré, (2008), *Tax Culture: A Basic Concept for Tax Politics, Economic Analysis and Policy*, 2008, vol. 38, issue 1, 153-167

¹⁰ Bruno Frey and Benno Torgler, *Tax morale and conditional cooperation*, *Journal of Comparative Economics*, 2007, vol. 35, issue 1, 136-159

¹¹ Philipp Doerrenberg & Andreas Peichl, 2010, *Progressive taxation and tax morale*, Springer Science and Business Media, LLC 2011

<i>Sociodemographic variables:</i>	<i>Socioeconomic variables:</i>
<p>Empirical studies provide evidence about the link between the tax morale and several individual characteristics, such as:</p>	<p>The studies which assess the impact of socioeconomic variables on tax moral mainly focus on:</p>
<ul style="list-style-type: none"> • age, • sex, • marital status, • religion, religiousness etc. 	<ul style="list-style-type: none"> • the level of individual's education, • the employment status and financial income.
<p>Based on a study about 17 European countries, Lago-Penas (2010) argue that those groups of individuals with a higher sensitivity for moral and ethics would, in turn, demonstrate higher tax morale. <u>Those are mainly religious people, as well as elderly and women.</u></p>	<p>Regarding <u>education</u>, some authors claim that the more educated people are, the greater the probability is to evade taxes. Others, on the other hand, claim that people with higher education can better recognize the benefits of paying taxes for the society, therefore the probability for tax evasion reduces with a higher level of education. (Torgler & Schneider, 2006; Frey & Torgler, 2007).</p>
	<p>Findings about <u>incomes</u> also differ. The major assumption is that individuals with higher incomes would rather evade taxes and in so doing will keep a greater portion of the income for themselves. Based on data from the European countries, Konrad and Qari (2009) have not provided evidence that incomes affect tax morale. On the other hand, Lago-Penas and Lago-Penas (2010) have found that the tax morale increases along with income growth due to the fact that tax payment reduces the financial stress.</p>

In addition to socioeconomic and demographic factors, there are also other contributing factors.

Trust in the government, the administration and the legal system: taking into consideration the fact that the behavior of the taxpayers tends to become regulated with “*clear rules*”, stable institutions and trust in the institutions may increase the tax morale (Torgler, 2001; Bird and et al., 2008). That means that trust in governmental institutions and legal systems will increase, by increasing the responsibility, the political stability and the absence of violence, as well as by the

efficiency of the government, the rule of law and control over corruption. McGee (2008) has concluded that the major argument in favor of tax evasion is that governments are susceptible to corruption and the tax system is unfair.

Democracy and national pride: By introducing democracy in the transition countries, the taxpayers are expected to get a democratic forum for decision-making (Feld & Frey, 2002). In a democratic environment of this type, it is assumed that tax revenues are spent based on the taxpayers' preferences, which increases tax moral. As a result of it, there may be a link between the pro-democratic views of individuals and the tax morale. Lago-Penas and Lago- Penas (2010) also find a strong positive effect of democracy on tax morale in 17 European countries.

Happiness and satisfaction with life: Happiness and the overall life satisfaction may serve as basis for higher tax morale. Frey and Stutzer (2002) claim that happiness may affect the economic decisions of individuals, such as their consumption, attitudes towards work, approach to investments etc.

According to Marcelo Bergman & Sven H. Steinmo (2018¹²), intimidation and putting pressure on citizens as a method of making taxpayers pay their taxes is applied only by weak countries.

Over the last couple of years, markets are suggested to be more efficient than countries, and in today's modern world the key issue is that countries have become too strong. The two authors believe that it is not all right and in their analysis they have pointed out that strong countries can instead demonstrate higher level of tax compliance.

Their analysis demonstrates clearly that only those countries which have managed to establish a two-way relation with their taxpayers and have thus managed to avoid the predator-victim relations can be considered strong.

The predator-victim attitude implies that the governments will obtain as they can by providing services and/or through extortions. In such predator countries, the country will provide minimum services with the purpose of justifying the revenues, while the victims, i.e. the taxpayers, will pay just the minimum amount so as to avoid sanctions. Based on this thorough study, the authors highlight multiple avenues for establishing a modern, efficient and successful tax system, and the conclusions they have drawn should not be taken for granted due to the fact that every tax system is specific. According to them, the Swedish example continues to be a model which can be copied, yet it is hard to believe that the Swedish example can be replicated or copied in its entirety.

However, key point that can be taken from the Swedish (but also the British and the American) model, unlike the Italian and the Romanian models, is the consent to paying taxes and the four major factors (which are presented in the following paragraph):

¹² Marcelo Bergman Sven H. Steinmo -The Leap of Faith: The Fiscal Foundations of Successful Government in Europe and America, Chapter 12- Taxation and Consent

- The country has to develop capacities for administering taxes that the citizens will consider as fair;
- Citizens are “prepared to pay” when they see that they get something in return and that other citizens are paying their taxes, too;
- Tax revenues are used for financing public programs and institutions which, in turn, contribute to greater social justice and equality. However, penal tax system aiming at imposing taxes at the rich, meanwhile offering them ways of evading it, generates little revenues and, at the same time, a lot of skepticism towards the state institutions;
- Those countries which manage to collect taxes and at the same time create a feeling of togetherness for the identity and the objectives, prove to be more successful.

Schneider, Buehn, and Montenegro (2010¹³) have assessed that revenues from economic activities which remain hidden from the tax authorities in the emerging countries (and weaker economies) amount to 36 percent of the GDP, while in the OECD countries with stronger economies, it amounts to 19 per cent. In their view, putting pressure and intimidating taxpayers is a very inefficient way of collecting revenues and will most probably generate high level of shadow economy and tax evasion.

Tax evasion has always existed into every single country, yet it is important to find ways of maximizing the level of tax compliance, meanwhile minimizing the level of deliberate non-compliance.

¹³ Schneider, Buehn, and Montenegro (2010)- Shadow economies all over the world : new estimates for 162 countries from 1999 to 2007. <http://documents.worldbank.org/curated/en/311991468037132740/Shadow-economies-all-over-the-world-new-estimates-for-162-countries-from-1999-to-2007>

2. Other Countries and their Experience with Tax Morale

A question raises as to why some people demonstrate greater readiness to pay taxes compared to others? In some countries, the government is ready to collect over 90% of taxes, while in other countries over 30% of tax revenues are lost due to tax evasion. Sven H. Steinmo (2018) has studied those questions in the thorough analysis *The Leap of Faith*, meanwhile analyzing the fiscal background of five various democratic nations: Sweden, Great Britain, Italy, USA and Romania. The analysis claims that the differences in voluntary tax compliance of citizens in various countries cannot be explained by the differences in policy cultures, but rather by the efficiency of the state institutions and the way they cooperate. In the analysis, the behavior of the taxpayers was tested in various societies in a situation when they face identical choices in the society.

Sweden¹⁴

According to Sven H. Steinmo (2018), Sweden may be the best example of a country which has established a strong balance in tax responsibility. The country is famous for having both the highest tax rates in the world and the highest level of tax responsibility and tax morale. The study has demonstrated that Swedish people are aware of the fact that they get a lot in return for the taxes they pay, and they have a high level of trust in their public institutions. However, the answer to the success of the Swedish example can be found in the sophisticated methods that the government has adopted for tracking the payment of taxes by their citizens. Furthermore, the reformed Swedish Lutheran Church has played the role of an agent who has assisted the state in gathering information about citizens and legitimizing the tax payments. Moreover, the military has made direct contribution to strengthening the horizontal agreement where the citizens had a feeling that the state owed them something. Finally, the major factor which has contributed the most to the success of the modern Swedish system is the concept of equity.

Italy¹⁵

While the church in Sweden has allied with the state in building a strong tax system, the church in Italy has done precisely the opposite. As Josef Hien (2018) has stated in *"Tax Evasion in Italy: A God-Given Right?"*, the catholic church has perceived the modernization of the Italian state as a competition. Instead of legitimizing the government activities and the tax authorities, the church servants in Italy were undermining the state and were even encouraging citizen to evade taxes as part of their moral duty.

Research has shown that Italy has produced opposite results compared to those of Sweden. The Italians are ready to pay their taxes provided that the money is shared and distributed in the system which they would consider as fair.

¹⁴ Marcelo Bergman Sven H. Steinmo -The Leap of Faith: The Fiscal Foundations of Successful Government in Europe and America

¹⁵ ibid

Nowadays, small business and their employees are extremely frustrated by the system which they had expected to be more efficient. The system in Italy is not only ineffective in terms of collecting revenues, but it also frustrates the citizens although it was supposed to be easy to administer. It is also publicly known that small businesses pay little taxes, which in turn encourages others to evade their taxes, too, and to have low level of trust in their government. In addition to it all, the repeated amnesty which several governments in Italy have granted to tax evaders has contributed to worsening the situation with tax collection by making citizens believe that the system will never be fair.

Great Britain¹⁶

Martin Daunton's (2001) analysis about the history of the British fiscal capacities is a case which ranks somewhere between the Swedish and the Italian case. Daunton puts his focus on the trust the British citizens demonstrate and the way the new British nations have managed to build institutions that will be trusted by the new generations. Great Britain was one of the first countries to become a tax state in the 18th century and collecting taxes with very low resistance by the citizens used to be one of the country's characteristics.

Although the British examples of the 17th and 18th century differed from the Swedish ones, they shared one common feature – just and legitimate method of tax collection. Taxes and tax calculations in Great Britain were done by the taxpayers themselves. Just as we could see in the case of Sweden, public legitimacy was based on the idea of an equal treatment of those with property and those with incomes. Justice and equal treatment were being applied hand in hand and, as a result of it, by the middle of the 20th century, in spite of some difficulties, the income tax had been embedded in the society. It has contributed to creating higher level of responsibility, trust in just taxes and widely accepted legitimacy of the state.

USA¹⁷

In the case of the USA, when compared to the Swedish and the British examples and taking into consideration the fragmentation of the federal tax system in the USA, suspicion may arise about the stability of the tax system compared to other countries. Furthermore, taking into consideration the movements for tax reduction (which have lately become specific to the US politics), one may expect that this country faces a high rate of tax evasion. However, tax morale is rather high in the USA, and taxes are paid regularly and without evasion in 85 percent of the cases. Therefore, the question we should ask is not why they have a high rate of tax evasion in the USA, but rather why it is so low. Many people would say that the answer lies in the authority that the Internal Revenue Office is granted, but the study of Romain Huret (2018) has demonstrated that the IRS authorizations did not play a vital role in the USA's tax collection efficiency model.

¹⁶ ibid

¹⁷ ibid

Romania¹⁸

Romania marks a low tax burden, flat income tax and the highest level of tax evasion in Europe, which helps us into seeing the difficulties in building trust in the government. Clara Volintiru (2018) and Arpad Todor's (2018) analysis have demonstrated how difficult it is to make citizens trust the system and the institutions when the government is corrupt and the institutions are inefficient. This analysis can help in understanding the dilemma the emerging countries are facing, and what is even more important, the experimental studies offer hope, especially due to the fact that it appears that the Romanians are ready to pay provided that they can trust the institutions that their money will be equally distributed.

Kosovo¹⁹

Just as in many other emerging countries, tax collection in Kosovo represents a challenge. Kosovo is one of the poorest countries in Europe regarding the GDP per capita. Not having an independent monetary policy, since the country has adopted the Euro as a national currency, it means that ensuring sustainable fiscal policy is of critical importance.

However, limited tax revenues represent a challenge for the government to deal with the economic cycles. Between 2011 and 2017, revenues amounted to 14% of the GDP, which is below the 19% average of the European and Central Asian countries^{20, 21}. Over 85 percent of the Kosovo government's revenues come from tax collection, and it is therefore very important to activate the collection of taxes from the perspective of increasing efficiency (and ensuring that taxes are collected at the lowest cost for the public administration) and from the capital perspective (ensuring that all taxpayers are reporting their incomes and paying their due taxes).

The effectiveness in the efforts to collect taxes depends on many factors. One of them is introducing the process for testing the commitment to paying taxes, learning from it and adapting the system based on the lessons learnt. This factor is equally important, just as the impact of the interventions on the revenue mobilization. The latest factor should be a long-term objective, which represents a function of changes in declarative behaviour.

In Marco Hernandez, Jonathan Karver, Mario Negre and Julie Perng's research (2019) Promoting Tax Compliance with Behavioral Insights, there are lessons learnt in two major fields from three experiments: 1) quality information systems, and 2) continuous communications infrastructure. Regardless of the resources which the tax administration has at disposal for access to and tracing of taxpayers, the inability for locating and contacting the taxpayers makes the collection hard. Therefore, one of the recommendations for efficient tax collection is launching a communication campaign through which taxpayers will be reminded of submitting their tax returns and paying their taxes on time.

¹⁸ Ibid.

¹⁹ Marco Hernandez (2019) - Jonathan Karver - Mario Negre - Julie Perng, Kosovo: Promoting Tax Compliance with Behavioral Insights

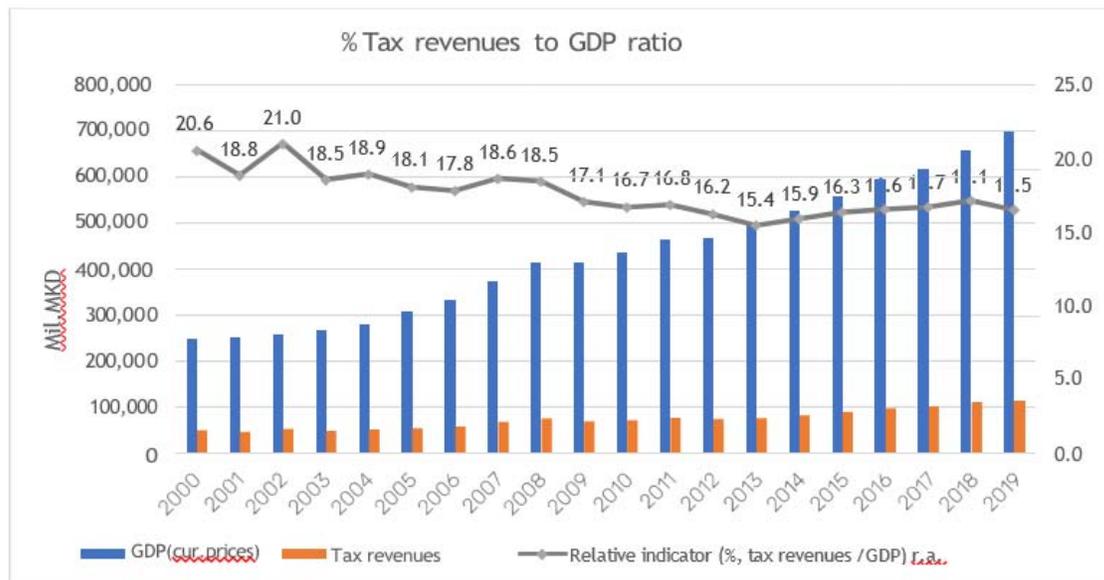
²⁰ Marcelo Bergman Sven H. Steinmo -The Leap of Faith: The Fiscal Foundations of Successful Government in Europe and America

3. Tax System in the Republic of North Macedonia

Public Revenues Structure

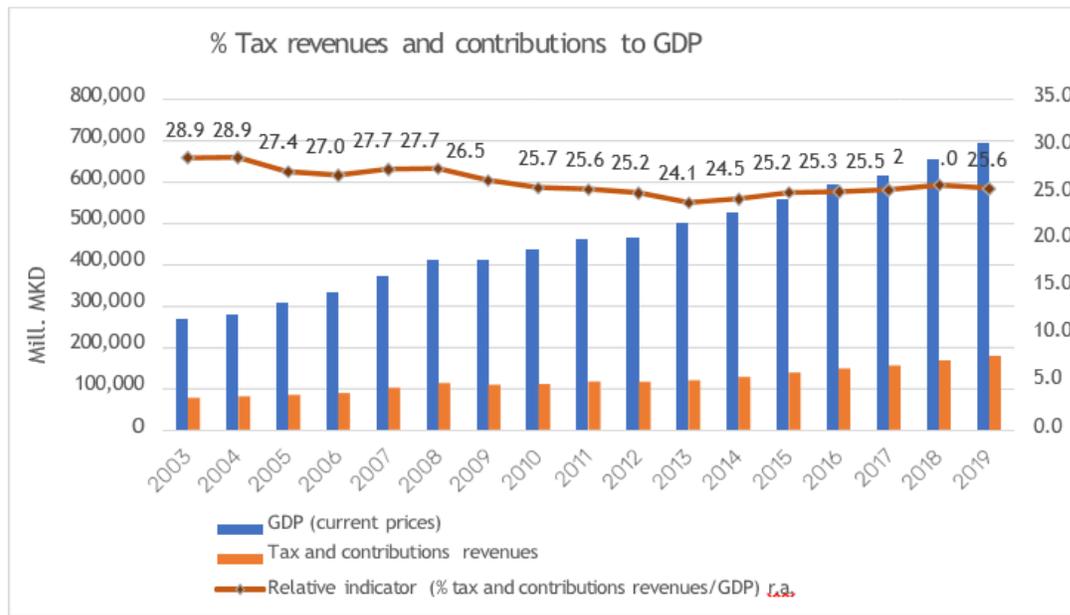
Total 2019 public revenues in the Republic of North Macedonia amounted to approximately 204 billion denars or 29.2 % of the GDP (GDP for 2019²²), while the 2018 relative ratio was 28.6 % of the GDP.

The relative tax revenues to GDP ratio is a simple measure of assessing the level to which taxes stimulate the national economy, and it is also used in combination with other metrics with the purpose of measuring the level of the government oversight over its economic resources.



Source: MF RNM data about GDP: (1) earlier data for 2018 2) evaluated data for 2019

Taxes, along with the social insurance contributions, account for the majority of the public revenues, making up 90.7% of the 2018 and 87,7% of the 2019 total public revenues.



Types of Taxes

There are direct taxes (wealth, revenues and profit) and indirect taxes (on goods with a shared burden between the seller and the purchaser). Types of taxes and contributions which fall in public revenues in the RNM are as follows: *personal income tax; profit tax; value added tax; excise duties; Customs – import duties; compulsory social security contributions (three funds); and property taxes (local taxes).*

Direct taxes

According to the applicable regulation (2020), in the Macedonian direct taxation system (income tax applicable to taxpayers as natural persons and profit tax applicable to taxpayers as legal entities), “flat” rate is applied to the personal income tax, as well as to profit tax – in both cases with 10 % tax rate.

The Law on Personal Income Tax²¹ shall regulate the taxation of natural persons’ income, the obligations of the taxpayer, the tax base for assessing the personal income tax, tax rates, payment deadlines and other issues which are significant for assessment and payment of the personal income tax. Personal income tax covers the following types of income in the country and abroad: 1) labor income; 2) income from independent activity; 3) income from property and property rights; 4) income from selling one’s own agricultural products; 5) income from industrial property rights; 6) rent and subrent income; 7) capital income; 8) capital gains; 9) gains from games of chance; 10) insurance gains and 11) other monetary, securities, in kind gains etc.²².

*Law on profit tax*²³ shall regulate profit taxation, tax rate, taxpayers, tax base for the profit tax, as well as payment deadlines, in addition to other significant issues related to

²¹ Law on personal income tax (Official gazette 241/2018 and 275/2019)

²² Article 1 and 2 of the Law on personal income tax (Official Gazette 241/2018 and 275/2019)

²³ Law on profit tax (Official gazette 112/14...248/2019)

profit tax assessment and payment. Profit taxpayers are legal entities and residents of the Republic of North Macedonia, who generate profit from doing business at home and abroad. The profit tax rate is 10%²⁴. The profit tax base is assessed as a difference between the taxpayer's total revenues and total expenditures, as regulated by the accounting standards²⁵.

“*Flat rate*” is a concept²⁶ whereby single tax rate is applied on natural persons' incomes, as well as on legal entities' profit above the established threshold or basic allowance. The Republic of North Macedonia was among the countries who have acquired this concept in the second wave of countries (after 2001, together with Serbia, Ukraine, Slovakia, Romania etc.), which followed after the first wave of countries from the Baltics (in 1994-1995²⁷), with some countries having ever since amended or completely abandoned this concept of taxation.

In the Republic of North Macedonia, the flat rate concept was introduced on January 1st 2007 at 12% rate which was reduced to 10% as of January 1st 2008. Except for the short period of time, when progressive tax was introduced in 2019^{28, 29}, „flat rate tax” with a 10% rate on personal income tax has been into force since 2008.

When it comes to profit tax, the 10% “flat rate” has been subject to some amendments in the period between 2009 and 2014³⁰ as a result of the relief measures due to the global financial crisis. Profit tax rate was reduced to 0%, i.e. the so-called Estonian model for profit taxation was applied, with only non-deductible expenses being subject to taxation, while the accounting profit is subject to taxation only if being distributed for dividend payment and other profit payments³¹.

Before 2006, the profit tax rate was proportionate to 15%, and in 2007 it was reduced to 12%. Regarding personal income tax, in the period prior to the flat rate, the tax rate was progressive, varying between 15%, 18% and 24%.

²⁴ Article 1, 2, 3 and 4 of the Law on profit tax (Official Gazette 112/14...248/2019)

²⁵ Article 7 of the Law on profit tax (Official Gazette 112/14...248/2019)

²⁶ The concept of flat rate is mainly linked to the academic work of Hall, R. E., and Rabushka, A. (1983), “Low Tax, Simple Tax, Flat Tax” (New York: McGraw Hill); 1985, “The Flat Tax” (Stanford: Hoover Institution Press)

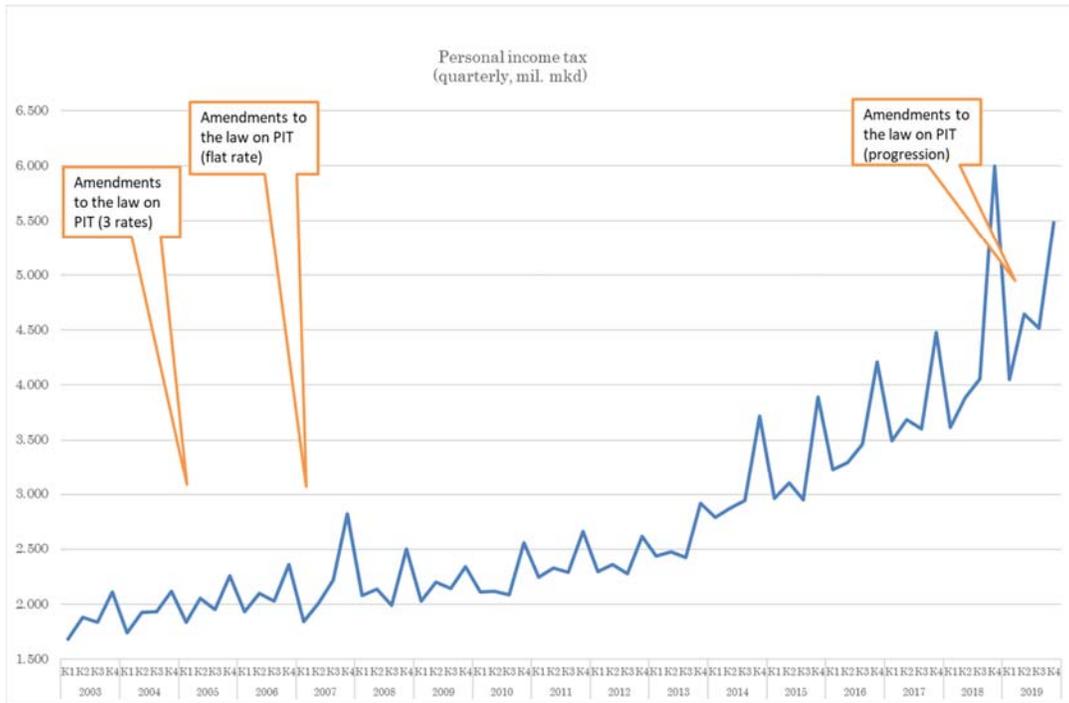
²⁷ www.ecb.europa.eu/pub/pdf/other/mb200709_focus10.en.pdf

²⁸ Law on personal income tax (Official gazette 241/2018)

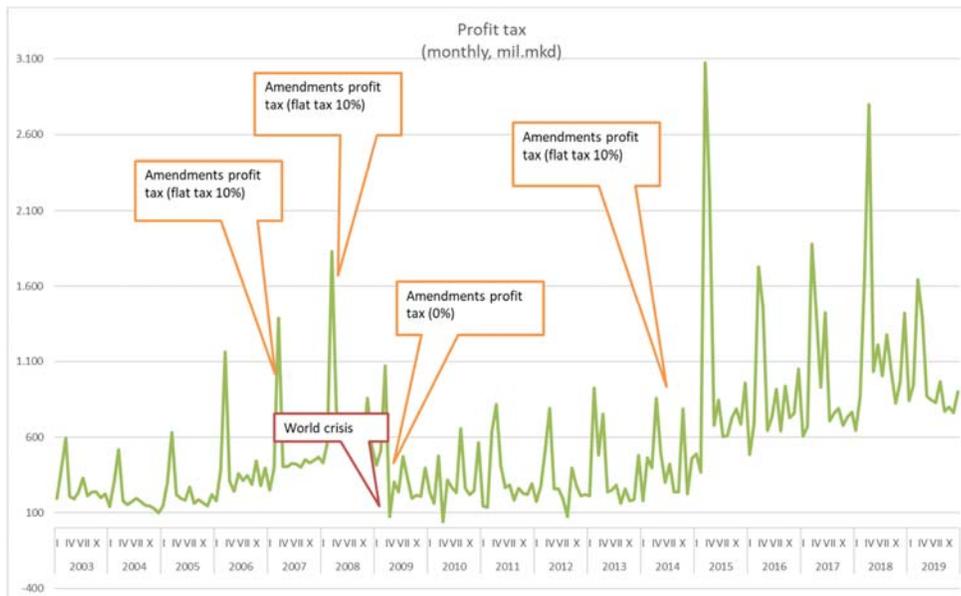
²⁹ Article 24 (applicable in 2020,2021,2022), from the Law on amendments to the law on personal income tax, (Official Gazette 275/2019)

³⁰ Official gazette of RM 13/2014

³¹ Article 36-g Law on amendments to the law on profit tax, (Official Gazette 159/2008)



Source: produced by the authors based on the treasury data and the amendments to the regulations



Source: produced by the authors based on the treasury data and the amendments to the regulations

A timeline of direct taxes

Persona Income Tax:

- ∇ 1994-2000:
 - Income amounting to 2 average monthly salaries (AMSs) was subject to 23% tax rate
 - Income between 2 and 5 AMSs was subject to 27% rate, and
 - Income above 5 AMSs was subject to 35% rate.
- ∇ 2001-2004:
 - Generated annual income below 360,000 MKD was subject to 15% tax rate, while incomes above 360,000 MKD were subject to 18% tax rate.
- ∇ 2005-2006:
 - Citizens' income was subject to three different tax rates: for an annual generated income below 360,000 MKD, 15% rate was applied,
 - for an income between 360,000 MKD and 720,000 MKD, 18% rate was applied, and
 - for an income above 720,000 MKD, 24% tax rate was applied.
- ∇ In 2007, personal income was calculated by applying the proportionate tax rate, i.e. the “flat rate”.
 - In 2007, personal income tax rate was 12%.
 - In 2008, personal income tax rate was reduced to 10%.
 - In 2009, by introducing the integrated tax payment and salary withholdings, the tax base for the generated annual income was reduced by the amount of the tax exemption of 84,000 MKD.
- ∇ In 2019 progressive tax rate was reintroduced. Additional rate on salaries and other personal incomes was applied as follows: 18% rate for incomes over 90,000 MKD, while capital incomes and games of chance rate was raised to 15%.
- ∇ In 2020, a 10% flat rate was reintroduced/freeze for a three-year period, and the progressive tax was on a standby (10% rate for personal incomes, 15% rate for games of chance)

Profit Tax:

- ∇ 1994 to 1996, profit tax rate was 30%.
- ∇ 1997 to 2006, profit tax rate was 15%.
- ∇ In 2007, profit tax rate, as established by the tax balance, was 12%.
- ∇ In 2008, profit tax rate was 10%.
- ∇ 2009 = 0% profit tax (Estonian model) or taxation only of the profit that was distributed as dividend,
- ∇ In 2014, the tax base for calculating profit tax was established by the profit that is subject to taxation (the difference between total revenues and total expenditures) being augmented by non-deductable expenditures.

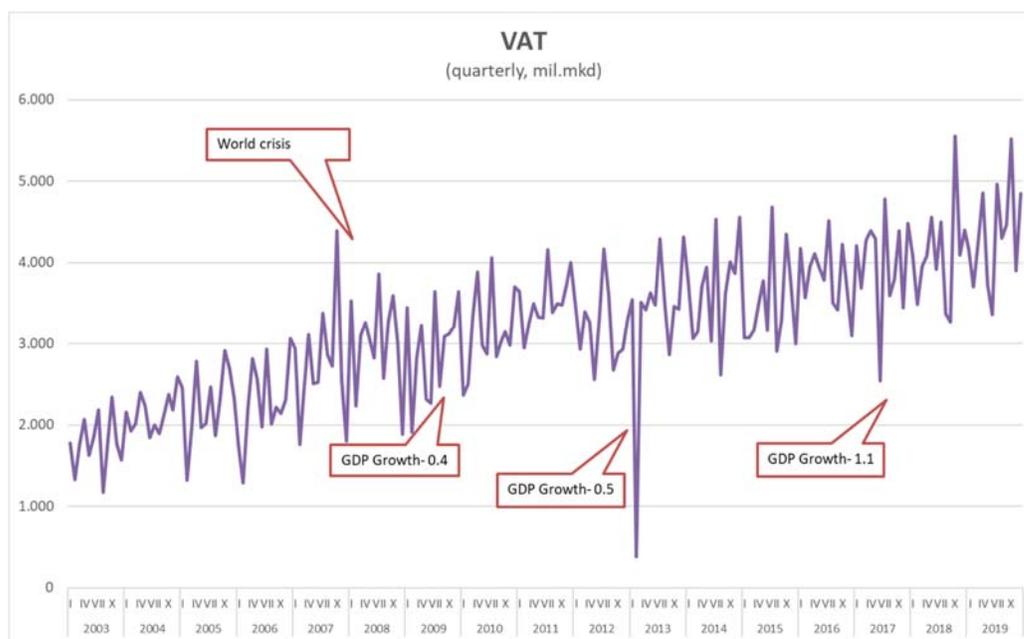
Indirect taxes

According to the law, *value added tax* is a general consumer tax, and it is being calculated and paid in all production and trade stages, as well as in the overall service sector. The following items are subject to value added taxation: 1. Commercial trade in goods and services in the country by taxpayers as part of their economic activity and 2. Import of goods³². The general value added tax rate is 18%, while the preferential rate of 5% is applied to certain goods and services (such as food, medicines, transportation, public utility services, accommodation services etc.). The Law on Value Added Tax entered into force in April, 2000 and it was introduced as a replacement for the Sales Tax. Over the last two decades, the law has undergone several amendments with the objective

³² Law on value added tax (Official Gazette of RM 44/99, ... 275/19)

of narrowing the space for tax avoidance, frauds and tax evasion. There were also amendments about the conditions for tax payment, assessment and adjustments to the annual turnover threshold for VAT payment. All of it was a part of the fiscal policy for stimulating the consumption of certain products.

The value added tax is represented with the largest share of 45.2% in the total tax revenues for 2019, i.e. 25.5% of the overall budget revenues.



Source: produced by the authors based on the treasury data and the amendments to the regulations

The law defines **Excise**³³ as duties for goods subject to excise (excise goods), and it shall regulate the manner of imposing, calculating and paying excise duties for the excise area of the Republic of North Macedonia. The Law shall also regulate the rights and obligations of excise payers, as well as the excise duties competent customs body, including also the procedure for monitoring of excise goods.

Alcohol, tobacco products, fuels and electricity are all considered as excise goods. Since the start of 2020, a new Law on Excise Goods came into effect, which exempts passenger vehicles from the Excise Goods Law, and moves it into the Law on passenger vehicles taxation³⁴ with the Customs Administration being in charge of its implementation. Since 2020, passenger vehicles are no more subject to excise duties, but rather to the passenger vehicle tax with a value component (ad valorem) and green component. The Law on Excise Goods was adopted in 2001 and in so doing, a legal regulation was introduced for excise goods storehouses, storage of excise goods, frauds and controls of excise goods movements, tax exemptions were reduced and mechanisms were introduced for keeping records and control³⁵. The excise payer is in possession of an excise permit, i.e. that is an entity which may import excise goods,

³³ Law on excise goods (Official gazette of the republic of North Macedonia 108/19 ... 275/19)

³⁴ Law on motor vehicle tax, Official gazette of the Republic of North Macedonia 261/19)

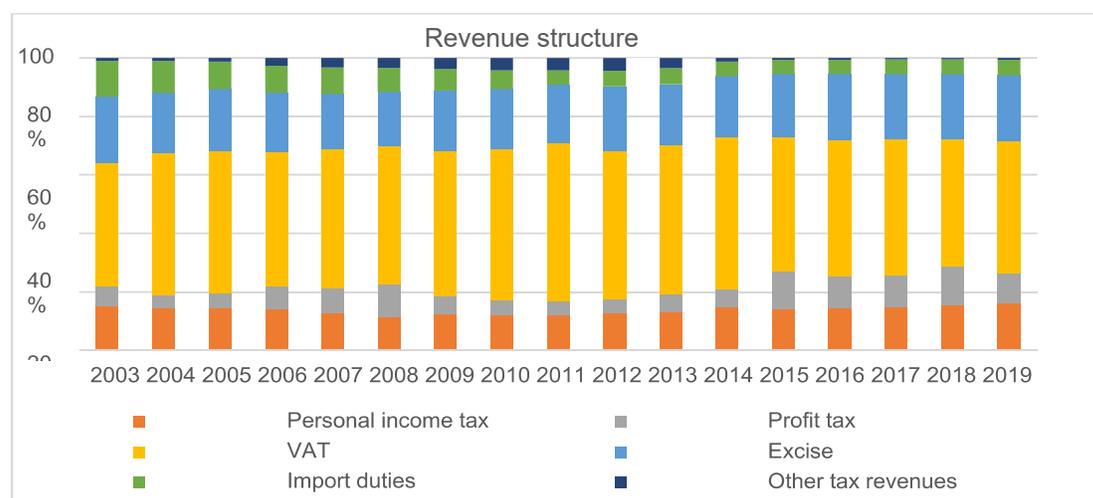
³⁵ Управа за јавни приходи на РСМ, <http://www.ujp.gov.mk>

or may produce or import goods that are subject to excise duties when excise stamps are being used, and the duties are paid directly or indirectly upon the consumption of a specific group of goods, i.e. excise goods such as mineral oils, alcohol and tobacco products (until last year passenger cars also fell into this group).

Excise goods duties are absolute per unit of measure (the so-called specific excise), while excise duties for tobacco products are paid as a combination of a specific and a proportionate excise duty (the so-called percentage excise). Excise duties account for 13% of the tax revenues for 2019 and 2018 (over the last two decades the excise duty share in the annual tax revenues ranged between 10.5%-13.4%).

Customs duties/Import duties – the Customs administration of the Republic of North Macedonia is the competent body for the implementation of the customs system. Customs operations are regulated by several laws, however customs duties are regulated by the Law on customs tariffs^{36,38}. Customs duties are imposed on imported goods as a protective function. Imported goods are subject to customs clearance, i.e. subject to taxation, the base of which is established depending on the value of the imported goods, and all the natural and legal entities which import goods are considered as duty payers (the law stipulates relief or exemptions for certain goods).

Customs rates in the Republic of North Macedonia are relatively low due to the high level of trade liberalization, as well as the obligations arising from the membership to the World Customs Administration and the Treaty for Stabilization and Association with the EU. In 2018 and 2019, import levies, i.e. customs duties accounted for 3% of the total budget revenues. The share of the import duties in the total revenues in the last two decades has dropped from 7% in the 2000s to around 3% in the 2010s, or in other words the import duties share in the total tax revenues is approximately 5% (in the last decade).



Source: produced by the authors based on data obtained from the Ministry of Finance of the RNM

³⁶ Закон за Царинска тарифа (Сл. Весник на РС Македонија 23/2003 ... 124/19.

Contributions from compulsory social insurance

Financial contributions are public expenditures for which the Ministry of Finance is the oversight body, and those assets are made available to the institutions for compulsory social insurance, which are established by laws regulating the compulsory social insurance system. The beneficiary of the contributions is considered as the payer, while the calculation and the payment of contributions is done by the employer (depending on the format, that can also apply to self-employed persons, individual farmers, clerics, state institution, a body or an organizer who has the obligation to calculate, withhold and pay the contributions on behalf of the beneficiary)^{37, 39}

Contributions from compulsory social insurance cover the following compulsory contributions: pension and disability insurance; compulsory capital-funded pension insurance; health insurance and unemployment insurance. The funds are made available to the National Health Insurance Fund, the National Pension and Disability Insurance Fund and the National Employment Agency.

The contributions from compulsory social insurance account for a rather large portion of the public revenues, with an almost constant 30% share in the overall budget revenues in the last two decades. The contributions from compulsory social insurance to GDP ratio in 2018 was 8.6%, and in 2019 it was 8.9% (the ratio has been varying between 8.4% and 8.9% over the last two decades). Contributions for pension and disability insurance, employment contributions and health contributions are calculated from the beneficiaries' gross salary base and represent revenues for specific funds which are used for financing current and future rights of the beneficiaries and represent a part of the RNM budget.

The current contributions from compulsory social insurance (as of January 1st 2020) amount to 28% of the gross salary, 18.8% of which are allocated for pension insurance, 6% are transferred to the second pillar (private pension associations), 7.5% for health insurance, 1.2% for unemployment insurance and 0.5% for additional health insurance.

□ Timeline of key changes to the compulsory social insurance system:

- 2009 Introduction of the Gross salary reform, including food and transportation allowance within the salary, reduction of the social contributions rate from 32% to 28.4%, reduction of the minimum base for calculating the social contributions from 65% to 50% of the average salary, as well as integrated payment of social insurance contributions and personal income tax in the PRO.
- 2011 Reduction in the social contributions rates to 27%
- July 2018 Reduction in the social contributions rates to 26,6%
- 2019 Increase in the social contributions rates to 27,5%
- 2020 Increase in the social contributions rates to 28%

Property Tax as part of Local Taxes

³⁷ Ministry of Finance of the Republic of North Macedonia, RNM MF, <https://finance.gov.mk/>

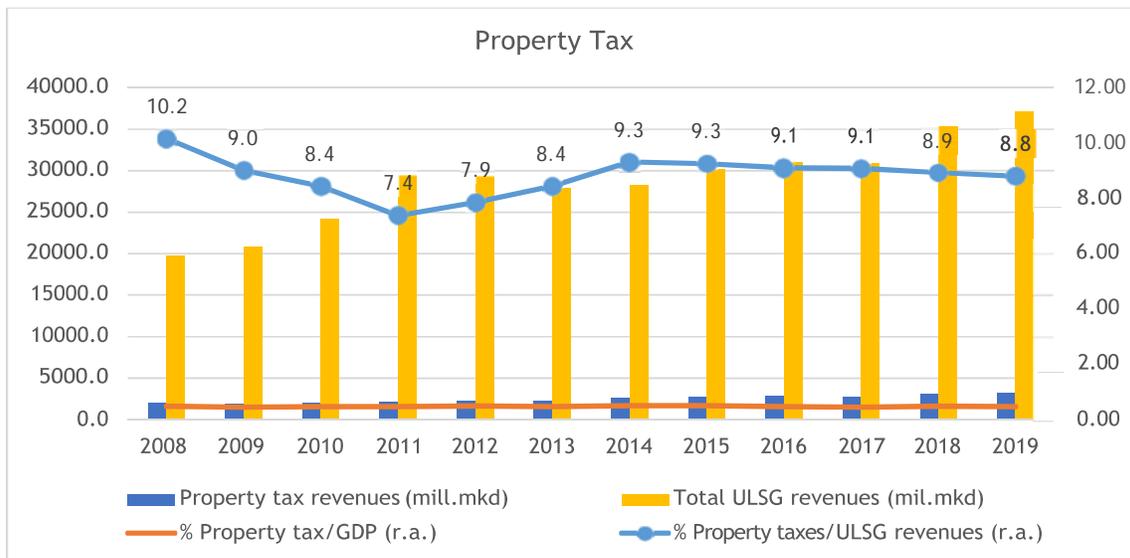
The Law on Property Tax³⁸ regulates the taxation of three types of property taxes. Property taxes are a source of municipal revenues and they are being fully administered by the units of local self-government. The Law on Property Tax covers three types of property taxes: 1) property tax (the rate ranging between 0.10% and 0.20% of the property market value, and is paid annually); 2) gift and inheritance tax (the rate ranging between 2% and 5% of the property market value); 3) real estate transfer tax (the rates ranging between 2% and 4%). The tax rates are established by every municipality individually and they have to be within the legal range (minimum and maximum threshold).

□ A timeline of key amendments to the property tax:

- ▽ 1994 as of 30/06/2005 and in line with the then applicable Law on property tax (adopted in 1993), assessment and collection of property tax, i.e. property tax, inheritance and gift tax and real estate transfer tax were conducted by the Public Revenue Office and the tax rates were fixed:
 - 1994-1997 tax rates were as follows: 0.10% for property tax, then inheritance and gift tax rates varied depending on the line of inheritance (inheritance and gift tax is not subject to taxation for the inheritor, i.e. first line inheritor, while second line inheritor was subject to 5% taxation rate and the third line of inheritor was subject to 10% tax rate), while the real estate transfer tax rate was 3%.
 - With the 1997 legal amendments, the tax rate for second and third line of inheritor was reduced to 3% and 5% respectively, while the provision about the calculation of movable property tax rate of 0.50% from its market value was revoked.
- ▽ Since 2005, with the process of decentralization and the new Law on property tax (which came into force on 01/07/2005), the competence for collection of property tax is transferred from the PRO to the units of local self-government.
 - The municipal administration is in charge of assessing and collecting property taxes
 - Tax rates are proportionate and, depending on the tax type, they are established by the Municipal Council, based on a Decision about the minimum and the maximum thresholds.

The overall property tax revenues collected by all the units of local self-government have been almost constant at a 0.5% of the GDP for the last decade (between 2008 and 2019 the share ranged from the lowest 0.45% to the highest 0.5% of the GDP). The amount of collected property tax revenues varies greatly from one municipality to another (and from one region to another) due to various factors, demography being one of them. The absolute values of property tax revenues for 2019 were 3.26 billion denars and they have been growing constantly in the last decade (starting with 2 billion in 2008).

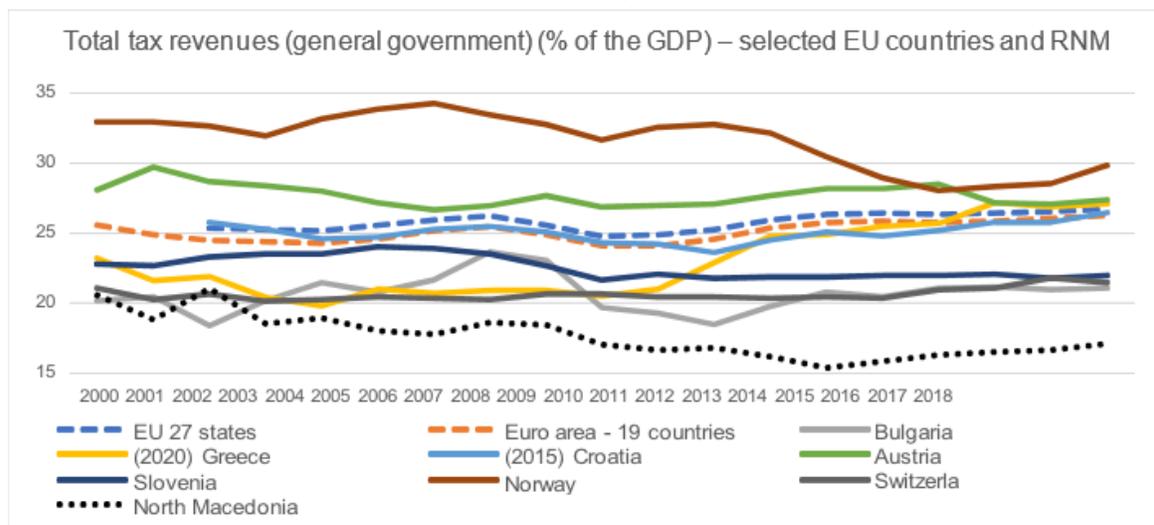
³⁸ Law on Property Tax (Official Gazette of the Republic of North Macedonia 61/04... 23/16



Source: RNM MF data, about GDP: (1) earlier data for 2018 2) assessed data for 2019

Tax Revenues to GDP Ratio and Comparison with Other Countries

Tax comparison³⁹, expressed as the relative ratio to the GDP, has demonstrated that the Republic of North Macedonia has a relatively lower ratio compared to the EU countries. The ratio of total tax revenues at the average EU level for 2018 was 26.8%, while in RNM this ratio was 17.1% for the same year.

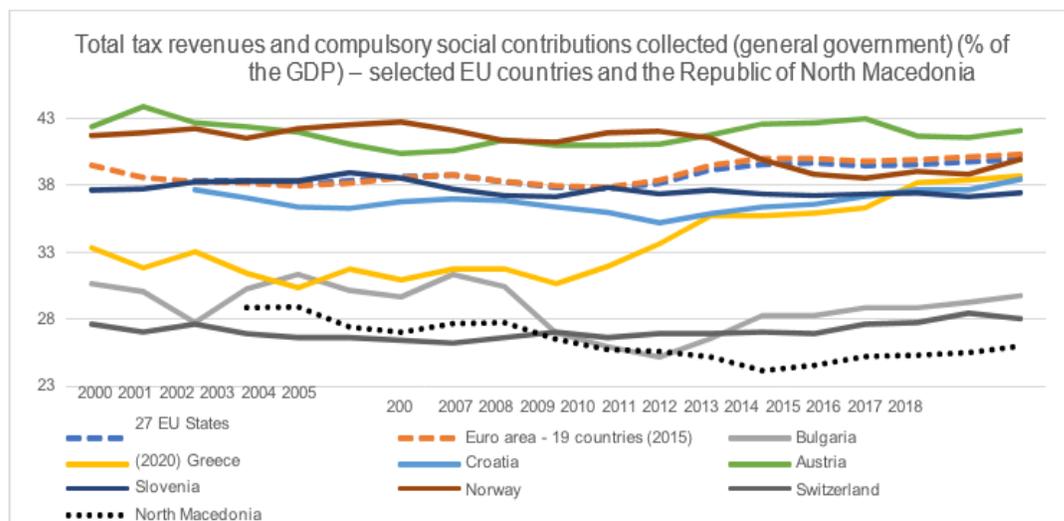


Source: EU countries EUROSTAT data, RNM MF data about the Republic of North Macedonia,

At the same time, the tax revenues ratio, including the revenues from compulsory social contributions for 2018, at EU level averaged to 40%, compared to the Macedonian average of 26%. The average relative ratio of tax revenues, including the

³⁹ Tax revenues to real GDP ratio, General government, Total tax receipts

revenues from compulsory social contributions, to the GDP at EU⁴⁰ level is marked with a stable positive growth over the last decade and differs depending on a country, with France, Denmark and Sweden having the highest level (over 43%), and Lithuania, Bulgaria, Switzerland, Romania and Ireland the lowest level (ranging between 30% and 22.5%).



Source: EU countries EUROSTAT data, RNM MF data about the Republic of North Macedonia

4. Rule of Law, Transparency and Trust in the Tax System

Many emerging countries are facing a series of challenges when it comes to increasing the revenues due to the low tax base, rather large informal sector, poor governance, low administrative capacities, low per capita incomes, low levels of domestic savings, investments and evasion of taxes. As a result of it all, two thirds of the least developed countries are still struggling to collect more than 15% of the GDP, being the widely accepted minimum for the effective functioning of the country. As a comparison, OECD member states increase their taxes, with the average being approximately 35% of the gross domestic product (GDP)⁴¹.

In the Republic of North Macedonia, the share of tax revenues in the gross domestic product (GDP) is around 17% (which has been almost constant for two decades) compared to the larger shares in the EU countries, ranging between 25-50%. This is the minimum level considered by the UN as necessary for achieving the Millennium development goal.⁴² For a comparison, the OECD countries tax revenues share in the GDP is approximately 35%.

In the case of RNM the indirect tax is dominant, i.e. around 80% falls onto consumption taxes (VAT), while in the EU personal taxes have a bigger share. Furthermore,

⁴⁰ Total receipts from taxes and compulsory social contributions after deduction of amounts assessed but unlikely to be collected. The indicators are compiled on a national accounts (ESA 2010) basis. They comprise detailed tax and social contribution receipts for the general government sector (S.13) and its subsectors (plus the Institutions of the EU (S.212), using the ESA 2010 classification

⁴¹ OECD (2019), Tax Morale: What Drives People and Businesses to Pay Tax?, OECD Publishing, Paris

⁴² United Nations –Millennium Development Goals <https://www.un.org/millenniumgoals/>

according to the estimations, the average contributing factor of evasion in the EU (indirect taxation and self-employment activities) is 14.5%.⁴⁵ Another study claims that the average tax evasion at EU level is 12,3% of the GDP or an average of 9,9%⁴³.

According to the abovementioned estimates, that means that the Republic of North Macedonia suffers losses of 9.9% of the GDP or 14.5%, which is 102 million euros annually due to the low tax morale (numbers that can go even higher in the Republic of North Macedonia if we take into consideration the likely lower level of tax morale as a result of the lack of trust in the state and local institutions).

Therefore, understanding the reasons for tax morale differences among countries is a key element which can help understand tax compliance.

This type of behavioral approach to tax system may offer more compared to the tax systems based on sanctions and the predator-victim model. For instance, personal reasons of taxpayers to either comply or not comply can be identified.

Better focus on tax morale provides for a pathway for voluntary tax compliance. Research has demonstrated a significant link between tax morale and informal economy, where morale is generally defined as an intrinsic motivation for paying taxes (Torgler, 2005).

Research in the field of political economy has identified the benefits of the “limited government”, but researchers have also been highlighting for a long time now the drawbacks occurring in the less developed nations as a result of the so-called “weak states” that lack power, credibility and trust to implement the process of taxation and to regulate economy, and in addition to that, they also lack power to sustain the political and social challenges coming from non-state actors⁴⁴.

The basic idea behind it is that when the government's participation is high, they impose very high taxes as a result of which the economic activities are suppressed. On the other hand, when the government's participation is low, they think that they will be unable to get the “rent” in the future and this is the reason for investment into public goods. There is a consensus about the belief that a strong country can correspond best to an OECD country where taxes are high in spite of the significant oversight by the society over the government. However, Steinmo in the Leap of faith argues that the opposite happens when it comes to tax compliance.

With the purpose of establishing the correlation between the power of the country and the fulfillment of obligations, we have attempted to answer the question by linking the percentage share of tax revenues in the GDP with the percentage share of the informal economy in the GDP, the result of which is -0.548. It indicates a slightly negative correlation and a statistical link between the countries with a lower level of informal economy which have higher tax shares in the GDP. This may indicate that to a certain degree the stronger countries which have the power for implementing the tax

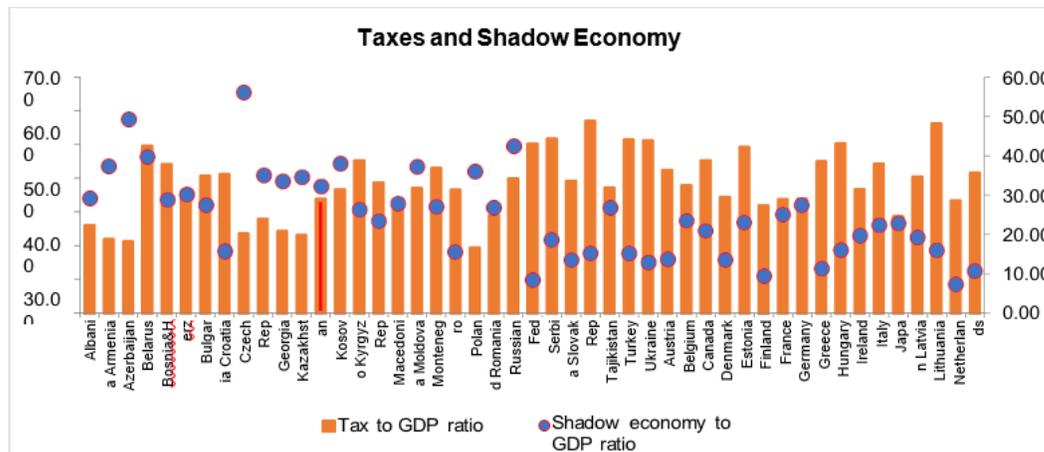
⁴³ The fiscal and social cost of tax evasion: the impact of underreporting of income by the self-employed
https://ec.europa.eu/jrc/sites/jrcsh/files/fairness__pb2019_taxevasion.pdf

⁴⁴ Taxation Trends in the European Union

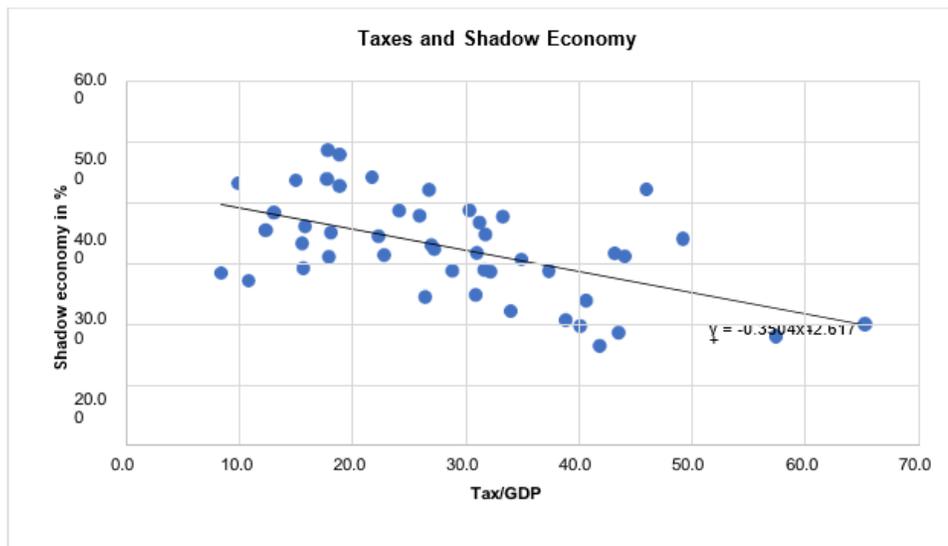
https://ec.europa.eu/taxation_customs/sites/taxation/files/resources/documents/taxation/gen_info/economic_analysis/tax_structures/2016/econ_analysis_report_2016.pdf Journal of Monetary Economics 52 (2005) 1199–1226 Politics and economics in weak and strong states, D., Acemoglu, MIT, USA, 2005, North, D.C., 1981. Structure and Change in Economic History. W.W. Norton & Co, New York.

regulation have lower informal economy, while the taxpayers are more tax compliant (and/or vice versa).

Shadow economy in the Republic of North Macedonia, which represents a rooted issue and continues to be a significant challenge, is something that CEA (2012) has studied, and the results indicate that it is present with over 30% in the GDP⁴⁵ in 2016. The IMF has also come up with 38% share of shadow economy in the GDP⁴⁶. This correlation confirms the view that a strong state, which has the power to implement its policies and whose citizens trust the system, is far more likely to have less shadow economy and, in turn, better tax compliance.



Source: Schneider 2010 study data, Revenue Potential, Tax Space, and Tax Gap a Comparative Analysis Munawer Sultan Khwaja Indira Iyer, 2014, World Bank, graph produced by authors



Source: Schneider 2010 study data, Revenue Potential, Tax Space, and Tax Gap a Comparative Analysis Munawer Sultan Khwaja Indira Iyer, 2014, World Bank, graph and correlation produced by authors

Tax morale is comprised of several interconnected elements. One of the approaches into

⁴⁵ For more information, see: Shadow economy in Macedonia, 2012, available at https://cea.org.mk/documents/studii/CEA%20SHADOW%20ECONOMY%20IN%20MACEDONIA%20FINAL_4.pdf

⁴⁶ 2019 Article iv consultation; Staff report; and statement by the executive director for North Macedonia, 2020, IMF

understanding the interconnections is proposed by the World Bank. The World Bank theory of change for tax compliance stresses the dynamic relations between trust, facilitation and implementation and their role into building tax morale. The theory argues that trust depends on the perception about the tax system being fair, just, reciprocal and accountable. As such, strengthening the tax compliance does not refer only to better forced collection, but rather to building trust, as well as credibility, fairness and just administration system.

According to the World Values Survey (Macedonia, 2001⁴⁷), ~ 5% of respondents stated that evading taxes is always justifiable, provided that one gets lucky to not be caught (unlike 66% who would never evade taxes and 29% who consider evading taxes justifiable to a certain degree). Furthermore, the same data has shown that 60% of the citizens agree with the increase of taxes, provided that the revenues be invested in solving the challenges such as the environmental pollution. The general conclusion from this survey is that citizens who consider democracy as the best system for the state government, have a tendency to think that evading taxes is unjustifiable.

According to the survey of the same research for 2020, there was again 5% of the respondents who considered tax frauds completely acceptable, while another 5% considered tax frauds somewhat acceptable. For 65% of the respondents, tax fraud was not acceptable at all, while another 20% stated that it was somewhat unacceptable. To sum it up, identical results after 20 years have demonstrated that the degree of acceptance of tax frauds has remained unchanged from a morale point of view.

Individuals who trust their governments have proven to have higher degree of tax morale compared to those who did not trust the government. Those citizens who consider fiscal redistribution as an essential feature of democracy, i.e. those who think that governments should collect taxes from the rich so as to subsidize the poor, have also demonstrated higher degree of tax morale compared to those who consider the concept of fiscal redistribution as insignificant. Those citizens who apply active engagement in decision making, in particular at a local level, have a higher degree of tax morale, a feeling of ownership and greater responsibility and accountability to the community and the society.⁴⁸

The system of public finances is expected to have transparent procedures and rules which will regulate the budget process and will also reflect the strategic planning of the budget process, whereby the executive branch will harmonize its objectives with the available resources from the budget. In theory, fully informed citizens create an environment for the politicians to be able to adopt socially optimal policies. Therefore, well set up procedures and rules, accompanied by transparency, lower the possibility for discretionary fiscal policies, as well as the trust in the governments.⁴⁹ The Government of the RNM often happens to exceed

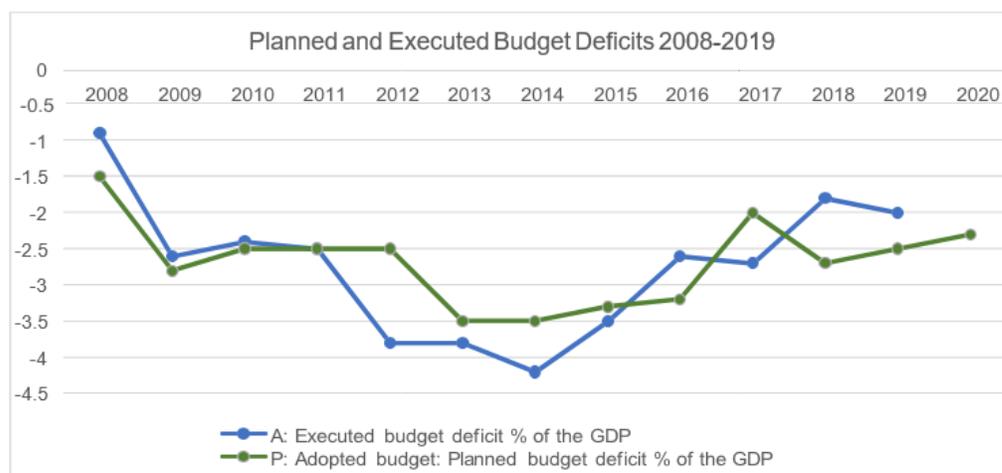
⁴⁷ World Value Survey —Macedonia 2001 <http://www.worldvaluessurvey.org/WVSDocumentationWV4.jsp?COUNTRY=508>

⁴⁸ *ibid*

⁴⁹ Center for Economic Analyses – Monitoring the budget expenditures before and during the election process

https://cea.org.mk/wp-content/uploads/2016/06/FINALEN-CEA-Izvestaj-CEA-TI_2.pdf

the deficit, particularly before the elections⁵⁰.



Source: Author's calculation of the Ministry of Finance data: <https://finance.gov.mk/>

Furthermore, capital expenditures get much more intensive before and during every election cycle, and they get stabilized and slightly reduced afterwards. Social transfers increase significantly before and during the elections.

CEA⁵¹ research has illustrated that the average annual overestimation of planned revenues between 2009 and 2015 is ~7% (the IMF has come up with the same results in its 2016 report), while the average of the planned expenditures between 2009 and 2015 was ~6%. The execution percentage of tax revenues is between 92% and 98%, while the numbers at the local level for local taxes are lower (although data is primarily collected centrally). For instance, all units of local self-government mark 91% of execution rate, while the local property tax execution rate is 82%, and other taxes and fees execution rate is 53% (2018 data)⁵².

Greater fiscal discipline is required for restoring the trust in fiscal authorities and, in turn, affecting positively the tax morale.

The trust index for the Government of the Republic of North Macedonia (according to the World Bank estimates)⁵⁶ scores 3/7 regarding the democratic status of the country, thus placing the country in the group of defective democracies (6,5/10 in 2018 with poorer scores since 2008 and being at the regional bottom), while the rule of law and citizen's participation index is about 6/10 for both items. Therefore, with this analysis we are trying to provide answers about the major drivers of tax morale in the country. In addition to this question, there is also the question of reverse causality, i.e. whether weak trust leads towards low tax morale or whether the low level of tax morale (among other aspects of civic responsibility) is the major driver of irresponsible governance.

Lack of responsible governance reflects upon many aspects of the country. From the aspect of public finances, the lack of discipline in implementing the plans for revenues

⁵⁰ ibid

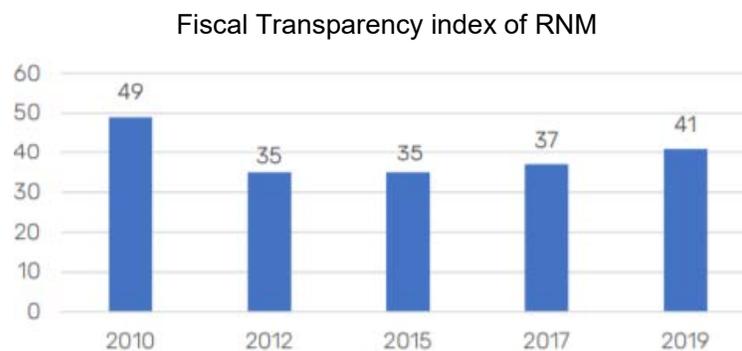
⁵¹ Ibid.

⁵² The World Bank, <https://qovdata360.worldbank.org/>

and expenditures becomes very apparent.

Research by International Budget Partnership⁵³ has demonstrated that transparency and open budget can help improve the socio-economic aspect. Open budget increases the fiscal transparency, as well as the accountability.

That can restore trust in the institutions and, thus, strengthen citizens' tax morale. However, according to the latest research, North Macedonia has continuously been improving the fiscal transparency since 2017, after the disastrous erosion of transparency measured in 2012. The Republic of North Macedonia provides sufficient data on fiscal policies in the draft-budgets, outlines the economic projections of the government and estimates the revenues, expenditures and borrowings. In 2019, for the first time in the cycle of the MPB methodology of measuring fiscal transparency in the Republic of North Macedonia, an audit was conducted not only by an independent expert, but also by the Ministry of Finance representative⁵⁴.



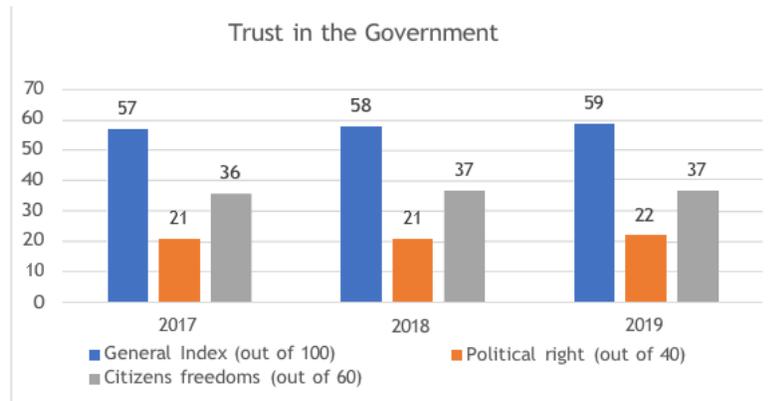
Source: International Budget Partnership

In addition to budget transparency and trust in the institutions, one of the contributing factors for trust in the institutions and tax morale is the level of corruption. According to Freedom House⁵⁵, “North Macedonia continues struggling with corruption and, in spite of the media and the civil society being active, journalists and activists have been facing pressure and threats. Corruption continues to be a serious issue with a prevalent grand corruption impunity for government officials, including members of the parliament and the judiciary. The government has made promises to undertake reforms with the purpose of increasing government transparency, yet progress is still to be made tangible. The latest 2020 report is yet to be published.

⁵³ International Budget Partnership <https://www.internationalbudget.org/>

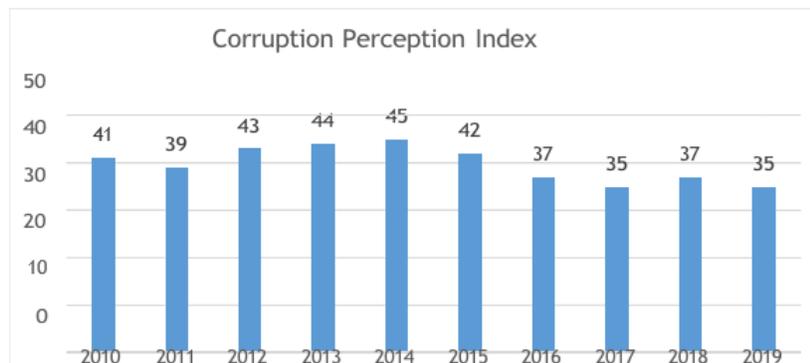
⁵⁴ Open Budget Index North Macedonia <https://cea.org.mk/severna-makedonija-go-podobri-svoeto-megunarodno-rangirane-vo-budhetska-transparentnost/>

⁵⁵ Freedom House- Report for North Macedonia <https://freedomhouse.org/country/north-macedonia/freedom-world/2019>³¹



Source: Freedom House

According to Transparency International⁵⁶, the Republic of North Macedonia has been lagging behind in the Corruption Perception Index, being ranked 106 out of 180 countries, compared to the last year's index when the country was ranked 93th. „With this ranking, the country is back at the 2017 score, when it was believed that the trust in the institutions was at the lowest level, yet the current results are just as same. The measures that were undertaken are not realistic, do not bring results and they point to the impact of politics on business and vice versa, the impact of business onto politics⁵⁷." Unless corruption cases are adjudicated, citizens may lose trust in the judiciary, which may, in turn, discourage taxpayers from tax compliance. In other words, higher level of corruption may impact negatively on the tax morale.



Source: Transparency International

The rule of law is the major reason for the citizens of the Republic of North Macedonia to be concerned. Indeed, this is an empirical fact that has been established by international factors. The perception about better rule of law with the assistance of the awakened civic stratum, has improved after the replacement of the government with the political proponent of a captured state in 2017. However, the recidivism of such rule still threatens the rule of law, and the vague legislation and arbitrariness of its implementation, along with the implementation of the taxpayers' rights, all of it still representing a challenge. The rule of law should provide an environment for efficient

⁵⁶ Corruption Perception Index <https://tradingeconomics.com/macedonia/corruption-index>

⁵⁷ Transparency International Macedonia: <https://bit.ly/2XyZuNt>

market economy, economic growth and development, while the public finance system should rely on transparent rules and procedures with the purpose of cutting the possibility for discretionary rule. The recent case of interpreting some provisions of the Law on Value Added Tax (VAT), as well as the attempt of applying it on natural persons in the absence of rules and procedure and in the presence of the tax base and legal incidence, serves as an example for the lack of rule of law or its distortion⁵⁸.⁶² Different interpretations of laws, frequent amendments to the legislation, inconsistent implementation of the laws or eroded rule of law may lead to weakening both the tax morale and the trust in the efficient utilization of the public finances.

In addition to transparency, institutional trust, rule of law and corruption level, the overall life satisfaction may affect tax morale, as well. Namely, happiness and life satisfaction may have a positive influence on tax morale, with happiness being one of the factors that affect the individuals' economic decisions, such as their consumption, their attitude towards work or how they perceive investments. According to the 2016 World Happiness Index, the Republic of North Macedonia (5,175) is ranked 92nd from a total of 155 countries on the list and 8th among the 10 countries of the region. Despite the fact that Macedonia is ranked somewhere in the middle between the index of the happiest country (Norway: 7,537) and the index of the least happy country (Central African Republic: 2,693) in the world, it still falls in the group of not so happy countries in the region, together with Montenegro and Greece. From the countries in the region, Romania and Serbia are considered as the happiest. Happiness and subjective citizens' wellbeing are key indicators of a country for measuring the quality of human development. Due to increased interest, many governments, communities and organizations use the determinants data from the happiness index, as well as the findings from the research on the subjective wellbeing in creating policies in favor of happier life.



Source: Center for Economic Analyses⁵⁹

⁵⁸ Natural persons in the VAT system and the rule of law in Macedonia <https://cea.org.mk/fizichkite-litsa-vo-sistemot-na-ddv-vladeeneto-na-pravoto-vo-makedonia/>

⁵⁹ The GDP fetish in Macedonia https://cea.org.mk/wp-content/uploads/2017/10/GDP_Fetis-vo-RM_WEB.pdf

5. Tax Morale Factor Analysis in the Republic of North Macedonia: Taxpayers' Opinion

In this part, we will refer to the above illustrated research and we will also try to compare it to the results from the field research on a relevant sample in RNM. The field research of a relevant sample in the RNM, which was conducted within this project by INDAGO, provides answers about the perception of the population in the RNM about:

- The functioning of the tax system in the RNM,
- Citizens' opinions about taxes,
- How informed people are about taxes and tax system and
- Citizens' trust in the institutions when it comes to spending public funds from collecting taxes.

According to the research, taxpayers in the Republic of North Macedonia consider themselves as not being well-informed about the types of taxes, and they also face challenges about differentiating local from central taxes. The knowledge about types of taxes, especially the difference between local and central taxes, is very important in the process of building civil society and citizens' participation in adopting public policies, mostly at local level.

Ignorance or misinterpretation may lead to an improper implementation of tax regulations and it can be a potential source for tax avoidance or tax evasion, i.e. tax non-compliance. However, in spite of the lack of information about types of taxes, taxpayers who have had experience and obligations for paying certain types of taxes, have stated that tax payment procedures are simple or very simple. Therefore, it is of paramount importance to increase fiscal transparency which had been eroded for almost a decade now in the RNM.

In 2020, research about transparent budget has demonstrated that the RNM has improved its fiscal transparency, yet there is still room for improvement, especially when it comes to citizens' participation in public finances (the RNM was ranked zero about citizens' participation in the budget process and the budget cycle, CEA 2020⁶⁰).

One of the taxes that an average taxpayer has to deal with is property tax. Since it is a local tax, every ULSG issues annual property tax statement, with one or two notifications for those who have not paid their taxes. The statement and the notification are submitted to every taxpayer in hard copy, which makes the tax visible for citizens and also makes citizens best informed about this type of tax.

Taxpayers have pointed to the need for having an additional information channel, such as a local office or a hotline, which can offer additional information about the type of taxes, procedures, deadlines, means of payment, as well as the distribution of collected taxes. Simple payment and tax reporting procedures is one of the factors

⁶⁰ CEA 2020, International Budget Partnership: <https://cea.org.mk/severna-makedonija-go-podobri-svoeto-megunarodno-rangiranje-vo-budhetska-transparentnost/>

that contribute to citizens' paying their taxes in timely fashion. Confusion about tax obligations may create a feeling of repulsion and delay in tax payment.

The taxpayers have expressed high level of moral values and they perceive themselves as responsible taxpayers who always pay their taxes on time. Being led by the social aspect, they believe to a certain degree that those with lower incomes have to pay lower taxes, and even if there is a chance for tax evasion, that would not be their primary option. If asked, the respondents are always in favor of reducing the tax rates for all tax types. The development level of individual moral values has certain effects on tax morale. If an individual nurtures moral values, they will reflect on responsibility for tax payment (as illustrated above in a research by Doerrenberg 2010).

The taxpayers demonstrate their distrust for institutions both at local and at central level, meanwhile demonstrating high level of distrust about the distribution of tax funds allocated for promoting public services. Based on their views, it becomes apparent that citizens consider capital investments as a priority for spending tax money, and they also consider that they lack information about the spending of public revenues, i.e. tax revenues, and they prefer more tangible capital investments. According to the citizens, some of the major priorities for tax revenues investment at local level are as follows:

- utility services
- roads and infrastructure
- local economic development,

At a central level, some of the major priorities for tax revenues investment are as follows:

- healthcare,
- roads and
- capital investments.

Moreover, the citizens are against tax increase, and besides that, they are also in favor of progressive tax rates, which they consider as fairer. It demonstrates that taxpayers are requesting greater fiscal legitimacy, better distribution of tax revenues, capital projects investments, and they would simultaneously like to have a more transparent and clear public finances system tailored to their needs.

Taxpayers tend to distrust the idea of curbing corruption both at local and central level, since their perception is that the situation has remained unaltered and there is no progress, at least not for the last five years. Transparency International research has confirmed a deterioration in the corruption perception at national level⁶¹.⁶⁵

Taxpayers tend to distrust the belief that increase in tax rates, and consequently increase in tax revenues will result in better quality public services. On the contrary, the expectations are that the revenues will be misused.

What is particularly concerning is the survey finding about the respondents' choice of a country of living. Namely, they would choose to stay and live in the Republic of North

⁶¹ Corruption Perception Index <https://tradingeconomics.com/macedonia/corruption-index>

Macedonia, which has low level of institutional trust, but also lower tax rates, rather than living in a country with more developed economy (such as Germany or Sweden) where there is higher trust in the institutions and higher life quality, but higher tax rates, as well.

What is indicative in this situation is that there is an implicit resignation when it comes to choosing to live where taxes are lower disregarding lower trust in the institutions and lower life quality. The resignation derives from the shaken trust in the institutions on a long run and it represents a huge risk for the future of the country. Namely, distrust in the institutions is one of the contributing factors for tax morale. If citizens have a constant feeling that their funds are misused by the authorities, there is a risk of lowering the level of tax morale as an answer to the irresponsible spending of tax revenues.

As a consequence of the current views and perceptions of the taxpayers, there is a greater dissatisfaction by the level of the democratic system development in the country and its functioning.

The citizens have a feeling that they are treated more as voters, and less as public service users. Regarding persons who do not pay taxes, citizens have a general opinion that it is a misuse that has to be sanctioned. Citizens also expect that, in the long run, hard work can contribute to better life and more success. Rule of law and the functionality of the democratic system is another factor that contributes to citizens' tax morale. If sanctions for tax evasion are not applied, it can affect citizens' decision to pay their taxes regularly and in timely fashion.

Conclusions

Compared to the studies of other European countries or the countries which have invested many years into building their tax system, one can conclude that **the process of building our national tax culture, as well as building trust in the tax system, is still ongoing, and the trust is still developing**. This especially if we take into consideration the different interpretations of the existing legislation on tax objectives and the frequent amendments to the legislation regarding the individual taxes in the last years.

Tax morale and tax responsibility in North Macedonia can be concluded to be at a dissatisfactory level, in particular due to the fact that the government has also identified it as a challenge in its analysis. One of the identified findings in our analysis is that taxpayers are not prepared for a rise in tax rate, i.e. increasing the levies on the taxpayers has a strong effect on lowering their tax morale, as a result of which taxpayers become creative with finding solutions for avoiding the tax burden. Opening a bank account in a neighboring country and transferring their incomes in a foreign country, as well as transferring it to other (close) persons who are below the threshold for progressive taxation are only some of the creative solutions. That is why the concept of progressive taxation is put on standby until the rule of law is improved and until other preconditions for its re-introduction are created⁶².

On the other hand, just as we have seen in other countries, such as Sweden and Italy, as two completely different experiences, **trust in the institutions is particularly important when it comes to the taxpayers' willingness to voluntarily pay their taxes**. In other words, the greater the trust in the institutions is, the less the citizens need to look for solutions to avoid taxes. Taxes are the price which the citizens have to pay, so that the government can provide services on behalf of the citizens and for their wellbeing. That is why the taxpayers perceive the link with the country not only from the victim's point of view and something the predator is forcing them at, but also as a process of exchanging common interests.

The citizens would like to feel as service beneficiaries, rather than just as voters. In this regard, transparency and citizens' participation in the fiscal processes are of paramount importance. The citizens will certainly feel deceived if the taxes are not spent efficiently and in line with their needs. If the citizens think that their interests (preferences) are well represented in the policies, and if they have a feeling that they receive proper public services and goods, **their identification with the country is much stronger, and so is their preparedness to contribute to the state by paying their taxes on time**. On the other hand, an inefficient state with prevalent corruption may affect the citizens' good will for cooperation, i.e. it may impact negatively citizens' decision for tax compliance. **Unfortunately, most of the respondents who took part in the research concluded that they did not trust the state institutions neither at local nor at central level**. They also think that, in case

⁶² Ministry of Finance <https://finance.gov.mk/mk/node/830>

they were to pay higher taxes, those revenues can only be misused, rather than being invested in better quality services.

In the case of Sweden, the soldiers' direct contribution to the state has influenced greatly the feeling of identification and the sense of belonging to the state, as well as the perception that the state owns them something. **The inner feeling that the citizens are involved in the social life, such as in establishing and creating policies, has contributes to the stronger sense for tax responsibility. Giving a chance to the individuals to be involved in the decision making, creates a feeling of civic responsibility, since the taxpayers become aware of the importance to contribute to the public good.** However, according to our research, the citizens have a feeling that they are treated by the authorities mainly as voters, and less as partners or public service beneficiaries. Hence, the state institutions should consider strengthening/building the relations for increasing the trust in the state institutions, including the judiciary, which is responsible for the rule of law.

Italy is an example where repeated tax evasion amnesty granted to individuals by several governments has contributed to the deterioration of the tax collection because the citizens were convinced that the system would never be fair. Some things which are familiar in our society, and which may become repetitive, can additionally deteriorate the distrust in both judicial and executive power. **The general perception is that those citizens who evade taxes, have close ties with the ruling party and, regardless of all, any type of misuse should be sanctioned.**

The situation in the Republic of North Macedonia is similar to that of Romania, where tax evasion is at a rather high level, yet there are some experimental studies which offer certain hope because it seems that the Romanians are ready to pay provided that they trust the institutions for a fair collection and redistribution of revenues. Similar to this example, **taxpayers in the Republic of North Macedonia consider themselves as individuals with high moral values, who would accept the tax burden if the public funds are to be efficiently distributed by the state institutions.** Regardless of anything, the citizens still hope that hard work may contribute to better life and greater success.

The rule of law and the functioning of the democratic system are factors that affect strongly citizens' tax morale. If sanctions for tax evasion are not applied, it can impact negatively citizens' decision for paying their taxes in full and on time. **Focus on sanctions, rather than on motivating the citizens to have a sense of responsibility and a sense of belonging to the community, is typical of a weak country** (Marcelo Bergman 2018⁶³). In this occasion, we have to remind ourselves of the punitive PRO expeditions and inspection bodies in the RNM, which were misused for political and fiscal purposes, beyond the institutions' scope of operations and served as a major instrument of the captured country.

Bringing social justice is one of the observations of this research. In other words, a fair approach would be the one where individuals with higher incomes would have to pay higher taxes. Those with a relatively lower income should be assisted by

⁶³ Marcelo Bergman Sven H. Steinmo -The Leap of Faith: The Fiscal Foundations of Successful Government in Europe and America, Chapter 12- Taxation and Consent

those who are able to provide assistance. Progressive taxation allows the countries to collect taxes from individuals who have higher incomes, thus creating a more satisfied society. Taxes are used for financing education, healthcare services and other goods for people who are really in need of; Groups focused on tax justice are focused on limiting the volume of the tax legislation and the rules which are beneficial only to a small portion of the population – those who pay taxes, compared to the rest of the population. **In other words, tax justice is aimed at everyone fulfilling their civic responsibility – that is paying their share. However, it should be done without haste and not only with the purpose of fulfilling someone’s ideological and political objectives, but also by identifying the wealth categories, the tax subjects, tax base, thresholds, exemptions etc.**

One of the conclusions of this research is that taxpayers in the Republic of North Macedonia consider themselves as being uninformed regarding the types of taxes and have difficulties differentiating between local and central taxes. **Being uninformed or having misinterpretations can lead to an improper implementation of tax regulations for taxpayers, and it can become a potential source of tax avoidance or tax evasion.** The government is making efforts to improve the exchange of information between the tax authorities and other entities. They are also working on improving the overall transparency in relation to tax issues, as well as the e-services for the citizens. **The major objective of this priority is to improve the quality of the services the taxpayers receive by the tax authority, to increase the economic feasibility of the procedures, as well as to simplify and to accelerate their application and to reduce the administrative burden related to them.**

In addition to that, another conclusion would be that **the taxpayers have underlined the need and the usefulness of additional channels for information, such as local offices or hotlines which will provide additional information** about the types of taxes, the procedures, the deadlines, methods of payment, as well as about the distribution of the collected taxes, since it is rather challenging to understand and differentiate between it all. But, **one of the factors that affect citizens’ willingness for paying taxes is the simplified procedure for payment. Confusion about one’s tax obligations may create resignation and delayed payment of taxes.**

Recommendations for Public Policies

Tax morale and voluntary tax compliance are linked with institutional trust and effective communication with the citizens. This analysis deals with a spectrum of factors which impact the tax morale of the Republic of North Macedonia. A significant portion of the same factors are identified in the findings, studies and discussions in other countries and regions, regardless of the fact that they may differ in their tax systems, tax policies and backgrounds, as well as in their demography and socioeconomic characteristics.

The discussions and conclusions from the analysis enable us to identify determinants and potential areas for various stakeholders in the society who have to support the efforts for improving the tax morale and voluntary tax compliance by the taxpayers.

The tax morale determinants in the RNM are strongly linked and dependent on:

- The level of ***trust in the government, the administration and the legal system — the rule of law***
- The manner and the degree of the two-directional ***communication between the tax authorities and the citizens***, as well as their effective participation in decision making – *functional democracy*
- ***Transparency and accountability*** of the public finance system, including fiscal discipline, as well

Therefore, we have identified three groups of public policy recommendations that will contribute towards increasing the tax morale, tax responsibility, and voluntary tax compliance:

- 1) ***Establishing a credible, consistent, stable and just tax system with predictable regulations***
 - *Strong efforts are needed for promoting the rule of law through practicing a constant, clear and consistent tax system. It all goes hand in hand with the predictable and clear legal regulation which would be implemented non-selectively and would contribute to increasing the trust in the system, the tax morale and the tax responsibility.*
 - *Selectivity or amnesty for tax evasion contributes to a worse tax collection because such cases make the citizens believe that the system will never be just and fair. This can shake even more the trust in both the judiciary and the executive power, due to the general perception among the citizens that those who evade taxes have close ties with the government and the political parties.*

Through advanced rule of law in all the tax system areas, foundations are set for building trust in the government, as well as trust among the taxpayers and the tax authorities in the efforts for building a fair and just tax system, which is a precondition for tax morale, tax culture and citizens' tax responsibility,

2) *Better transparency of public finances in the Republic of North Macedonia, as well as promotion of fiscal discipline for better fiscal legitimacy:*

- *Better transparency of the tax revenues by establishing a clear link with the expenditures, which will help those citizens who are the most concerned about the lack of information on where their money is spent to have a clear information and, thus, increase their tax morale;*
- *Active, complete and clear briefing of the citizens about the public revenues and public expenditures, both at central and local level, since the citizens have a low level of trust for any level of the government and they also distrust the process of accountability for the public finances. Therefore, the perception about corruption would decrease, and it is directly linked to the trust in the government and tax morale.*
- *Establishing a system of a two-directional effective communication, whereby citizens would take active participation in the decision making for tax collection and identification of priorities for spending the public finances. Although there has been a progress in the general fiscal transparency, citizens' active participation in decision-making is at low level. Increasing citizens' effective participation in making decision and identifying priorities for spending public finances, will increase the sense of identity and belonging to the society, which in turn increases tax morale.*

By improving the transparency of the tax system and functional democracy, the citizens of the Republic of North Macedonia will fill less like being solely voters, and more like being beneficiaries of public services tailored to their needs and to the priorities in the community. In so doing, the fiscal legitimacy of the government will also improve in the perception of the citizens, who will remain assured that those taxes that are additionally collected will not be misused.

3) *Better services and greater efficiency in tax collection*

- *Tax authorities should create sufficient administrative capacities and additional channels and avenues of communication, through which taxpayers will be educated and informed about certain issues in the system and the processes;*
- *Improved electronic systems for taxpayers and tax authorities, which will*

provide better efficiency and will cut the administrative burden. It will also modernize the procedures for tax administration and, in doing so, will reduce the space for corruption and will improve „taxpayers' experience “.

- o *Create and update taxpayers' profiles by analyzing the views and the perceptions of the citizens regarding tax issues, which will help in providing more information for tax authorities and decision makers for specific groups about the socioeconomic, demographic and institutional factors that have an impact on the tax morale.*

ANNEX

Data Analysis of Public Opinions from the Study across Regions (Regional PRO Offices)

Methodology

The study was conducted between February 25 and March 8, 2020. A representative sample of 1,000 respondents (18+ years) was designed by interviewing the representative sample of citizens across the entire territory by using multi-layered random sampling units based on the probability proportionate to the population size. The number of primary sampling units in every stratum is proportionate to the size of the assessed population in the given stratum. Assessment of the population size was conducted based on the 2002 census and the latest 2017 population assessment. For the sake of the study objectives, the respondents were grouped into regional PROs, i.e. they were grouped into one of the six offices (RO Skopje, RO Tetovo, RO Bitola, RO Prilep, RO Shtip and RO Strumica).

Results across Regions (Regional PROs)

Annexed to this analysis are the results about every question and they are presented in the sections of the questionnaire. The results are presented for the total number of respondents and they are segregated by regional PROs (RO Skopje, RO Tetovo, RO Bitola, RO Prilep, RO Shtip and RO Strumica).

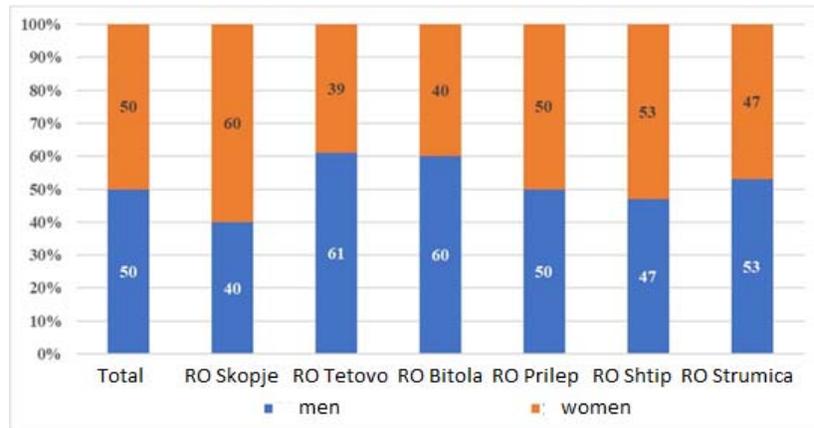
Annexed to this analysis are the results for every question presented in the sections of the questionnaire. The following text offers statistical processing of the average indicators for answers to certain topics by presenting the results for every question related to the regional distribution of taxpayers (regional PROs). The results are presented for the total number of respondents and they are segregated by regional PROs (RO Skopje, RO Tetovo, RO Bitola, RO Prilep, RO Shtip and RO Strumica).

Socioeconomic and Demographic Sample Features

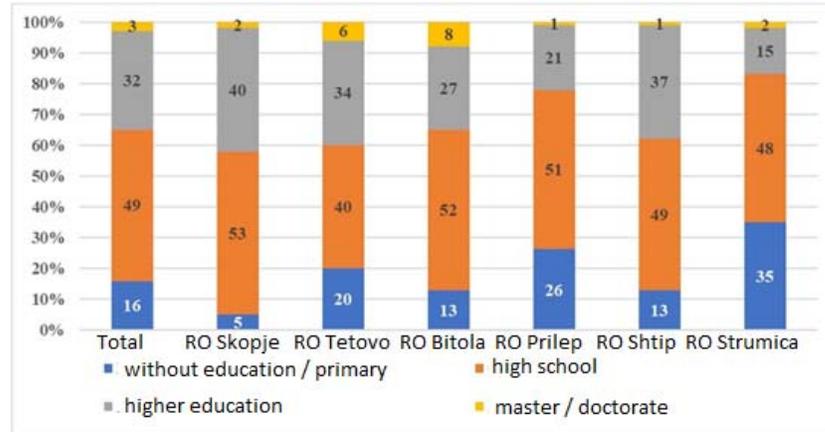
D1.Age-%



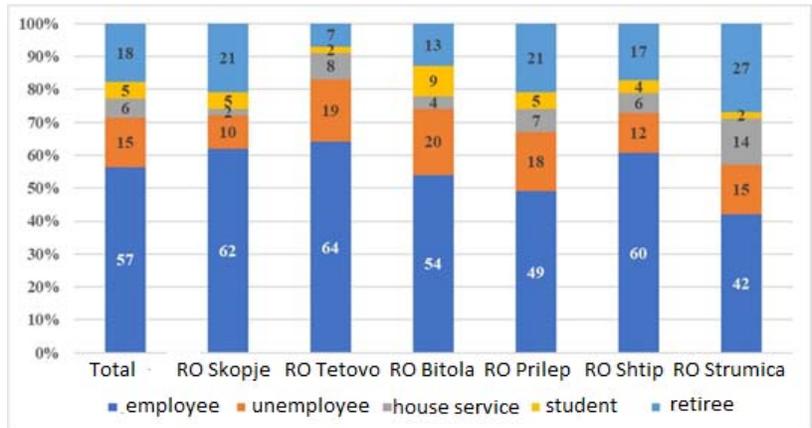
D2.Respondents' Sex -%



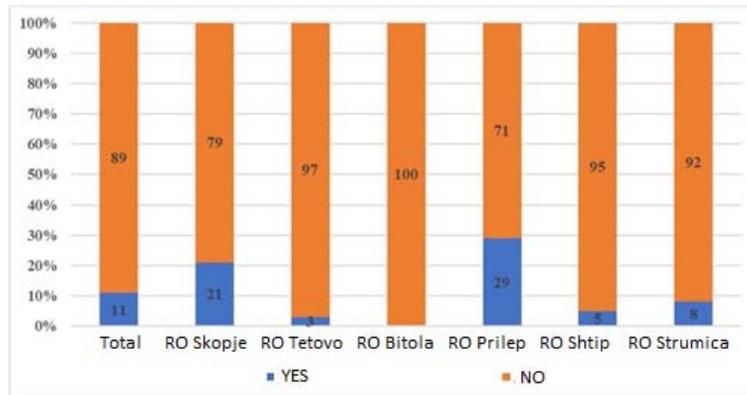
D3. Level of Education - %



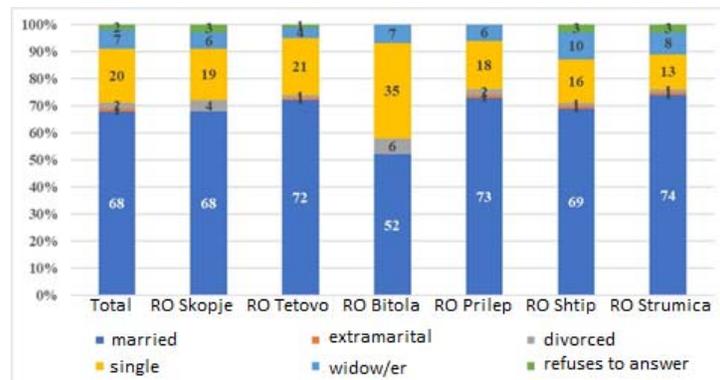
D4. Occupational Status - %



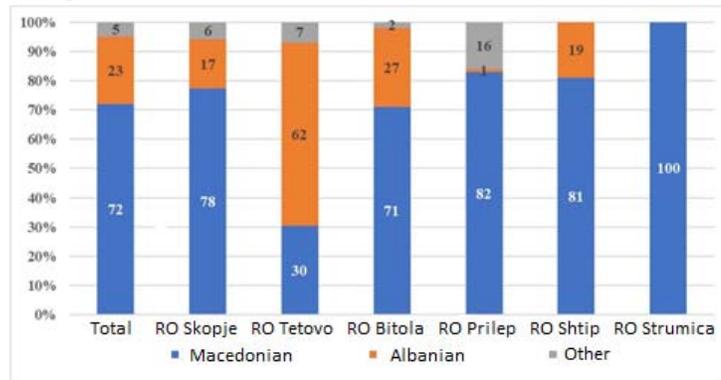
D5. Are you a welfare beneficiary? - % (Welfare beneficiaries, n=146)



D6. Marital Status - %

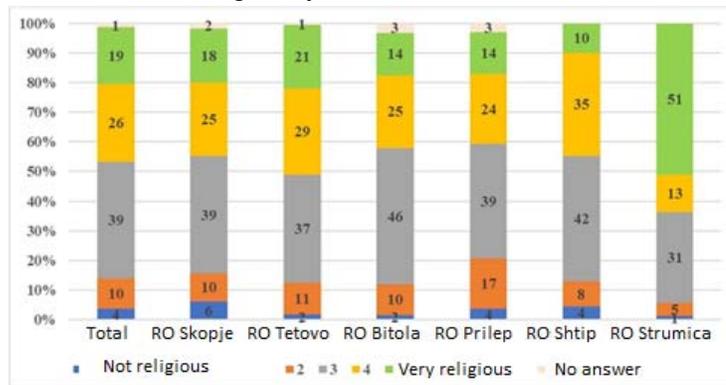


D7. Ethnic background - %



Religion

Question A51. On a scale of 1 to 5, with 1 meaning "I am not religious at all" and 5 meaning "I am very religious", please rate how religious you are? - %

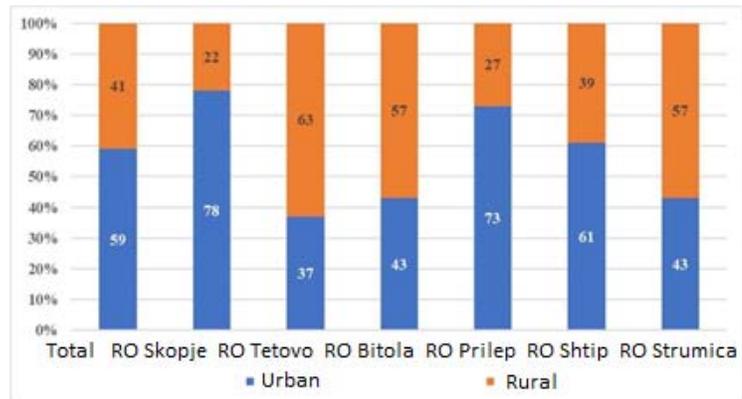


When it comes to religion, 45% of respondents stated that they were religious (4+5). The ROs with the largest number of religious respondents were the RO in Strumica and RO in Tetovo. RO with the highest percent of respondents who stated that they were not religious (1+2) are RO Prilep and RO Skopje.

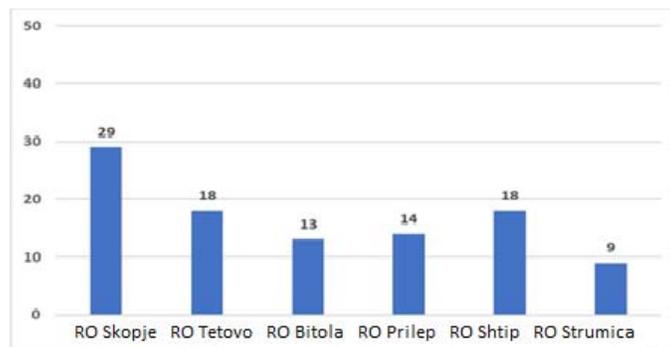
D8. Average Monthly Household Income - %



D9. Area (rural/urban) - %

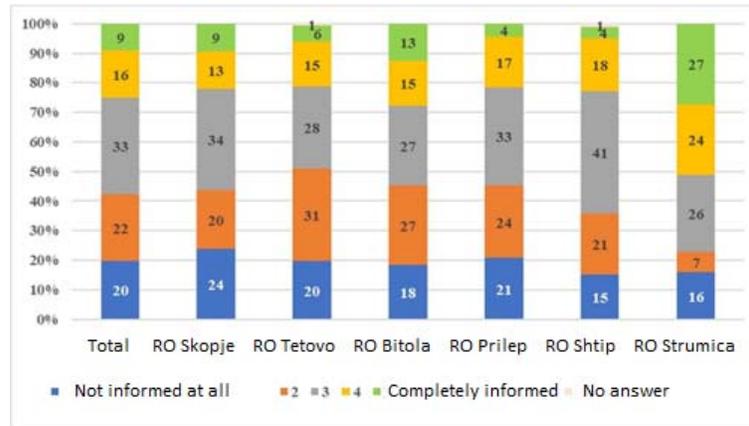


D10. Regional PROs - %



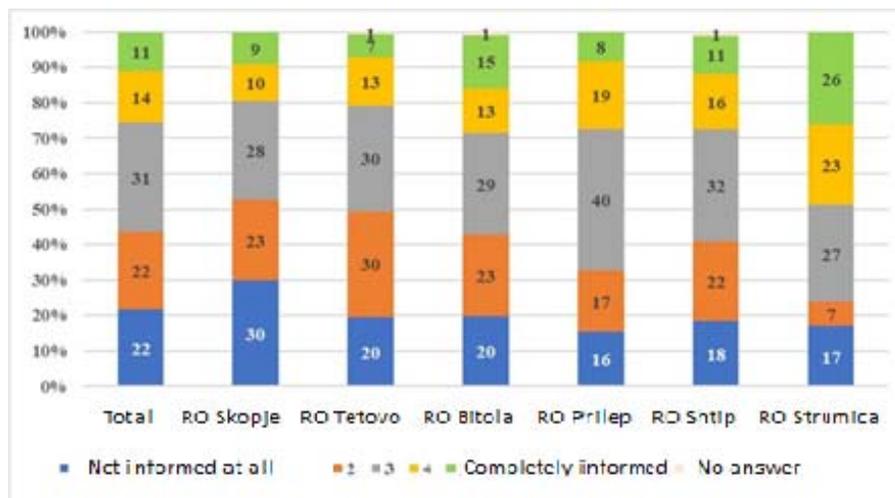
Being Informed about Taxes (Central and Local)

Question: A1. On a scale of 1 to 5, where 1 means "not informed at all" and 5 means "fully informed", how informed are you about central tax collection by the state? - %



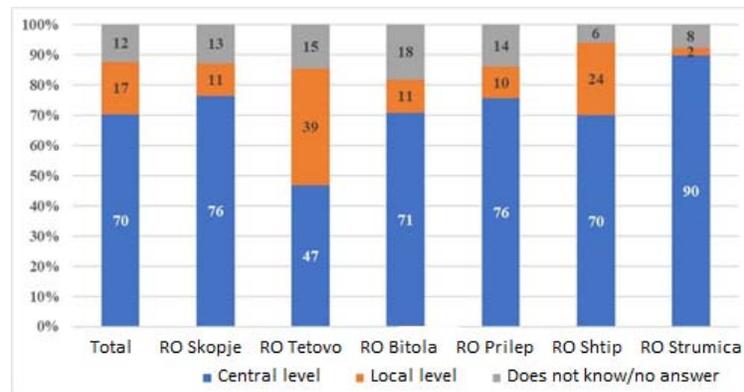
Result: The results have revealed that 25% of the respondents consider themselves as being informed (4+5) about central taxes. A majority of those who consider themselves as being informed come from RO Strumica, while the rest of the respondents consider themselves as less informed.

Question: A2. On a scale of 1 to 5, where 1 means "not informed at all" and 5 means "fully informed", how informed are you about taxes collected by the local self-government? - %



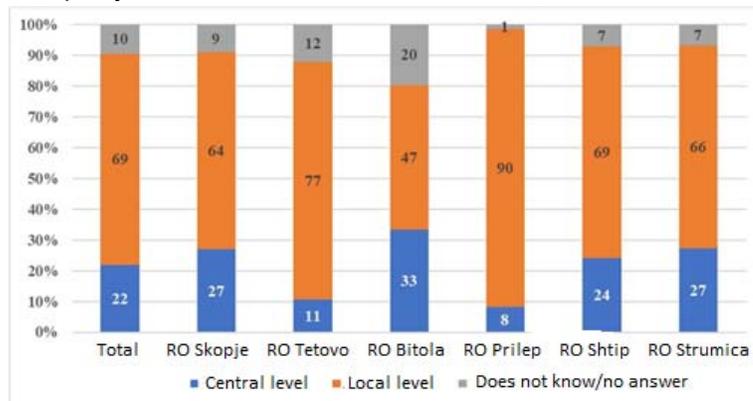
Result: The results have revealed that 25% of the respondents consider themselves as being informed (4+5) about taxes collected at local level. A majority of those who consider themselves as being informed come from RO Strumica, while the respondents from RO Tetovo and RO Skopje consider themselves as the least informed.

Question: A3. According to your opinion, which of the following taxes are collected at central level and which at local level? – Personal income tax %



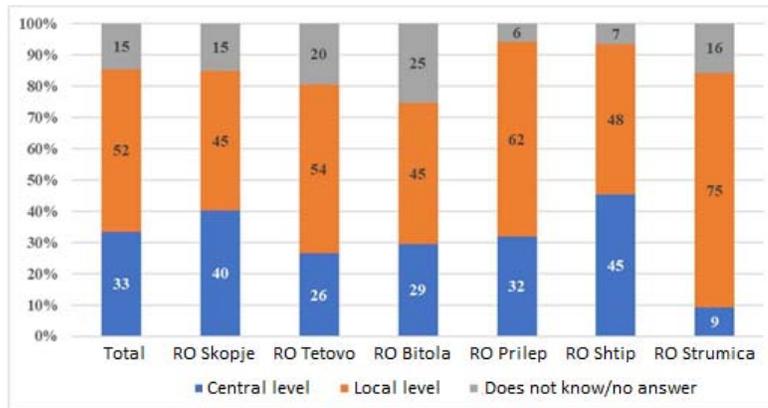
Result: Based on the data, 70% of the respondents think that personal income tax is collected at central level, the respondents from RO Tetovo being represented with the lowest percentage, while the respondents from RO Strumica being represented with the highest percentage.

Question: A3. In your view, which of the following taxes is collected at central level and which at local level? –Property tax %



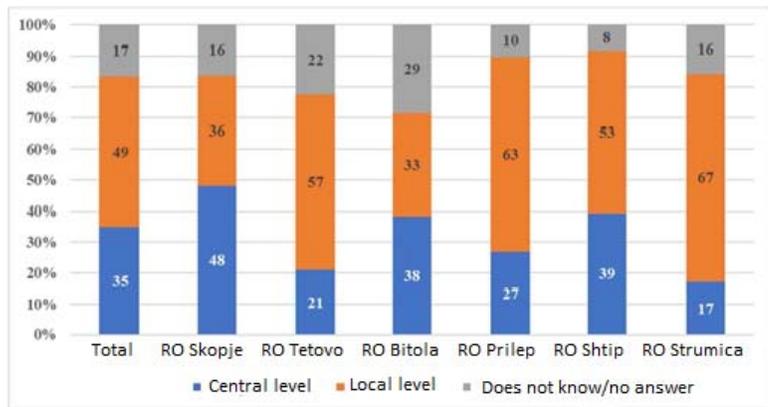
Result: The chart reveals that 69% of the respondents think that property tax is collected at local level, with the RO Bitola respondents being represented with the lowest percentage, while the RO Prilep respondents being presented with the highest percentage.

Question: A3. In your opinion, which of the following taxes is central and which is local?
 – Real estate transfer tax %



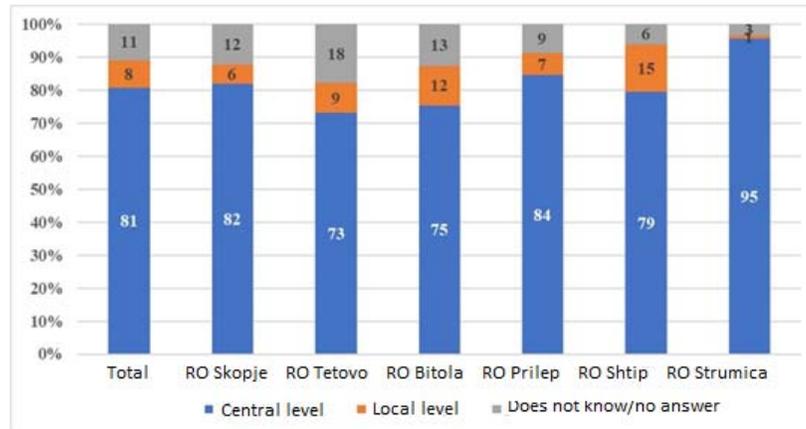
Result: The results have revealed that 52% of the respondents think that the real estate transfer tax is collected locally. The percentage of the respondents who consider it as local tax is the highest in RO Strumica and the lowest in RO Bitola and RO Skopje.

Question: A3. In your opinion, which of the following taxes is central and which is local?
 – Gift and Inheritance Tax %



Result: 49 % of the respondents think that the inheritance tax is collected locally. The percentage of the respondents who consider it as local is the highest in RO Strumica, and it is the lowest in RO Bitola.

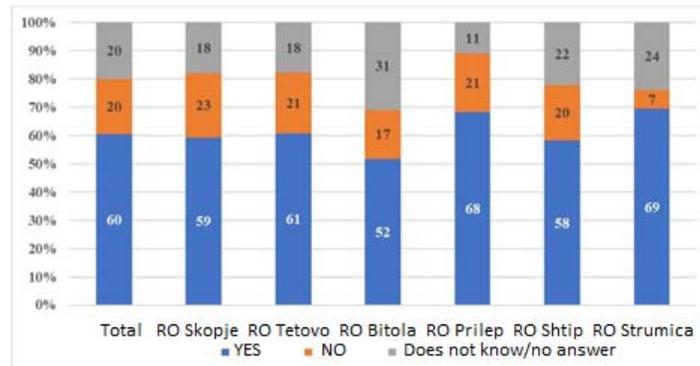
Question: A3. In your opinion, which of the following taxes is central and which is local?
 – Value added tax %



Result: 81 % of the respondents think that the value added tax is collected at central level. The percentage of respondents who consider it as central is the highest in RO Strumica and it is the lowest in RO Tetovo.

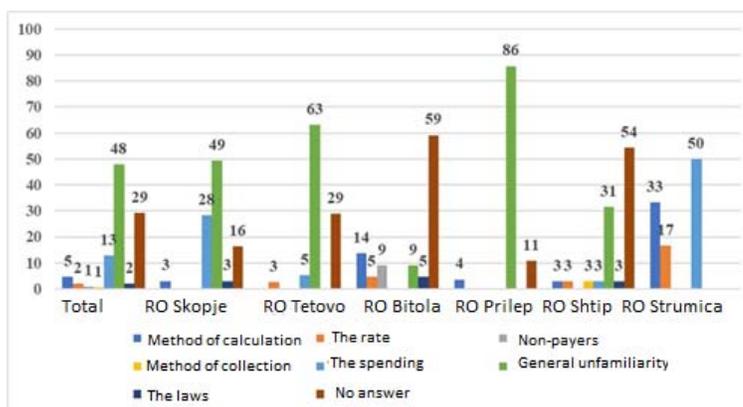
Opinions and views on tax procedures

Question: A4. Do you find the central tax payment system (e.g. laws, tax rates, taxpayers) clear? - %



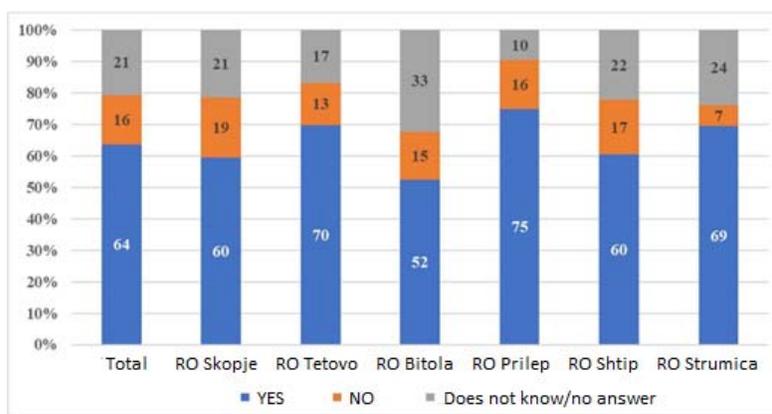
Result: About two thirds of the respondents (60%) think that the central tax payment system is clear. The percentage of the respondents who think that the system is clear is the highest in RO Strumica and RO Prilep, and it is the lowest in RO Bitola.

Question: A5. Please, let us know what is unclear? - % (Number of respondents who said that it was unclear, n=196)

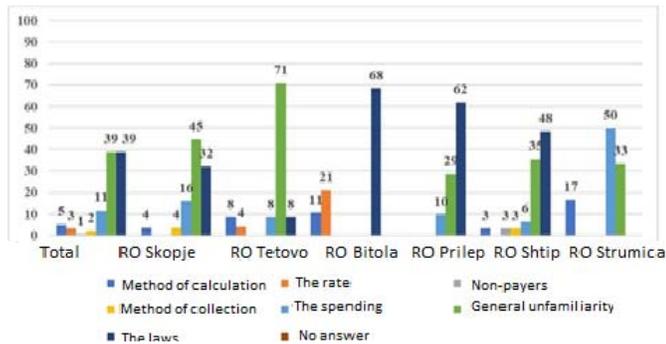


Result: A majority of the respondents (48%) stated that they were completely unfamiliar with the taxes collected at central level. Respondents from RO Prilep, RO Tetovo and RO Skopje are generally unfamiliar about taxes, while the RO Strumica respondents stated that they were unfamiliar with the spending. A majority of the respondents from RO Bitola and RO Shtip did not provide answers to this question.

Question: A6. Do you find the local tax payment system clear (eg. laws, tax rates, taxpayers)? - %



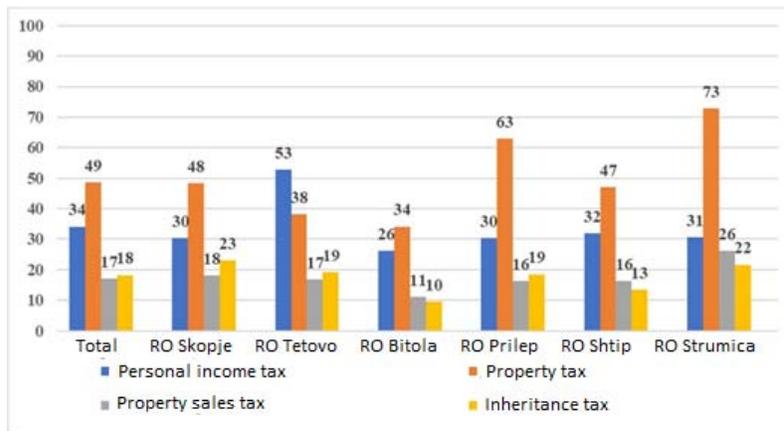
Result: Two thirds (64%) of the respondents think that the tax payment system at local level is clear. The percentage of respondents who think that the system is clear is the highest in RO Tetovo, RO Strumica and RO Prilep, while it is the lowest in RO Bitola.



Question: A7. Please, let us know what did you find unclear? - % (Respondents who stated that they found it unclear, n=157)

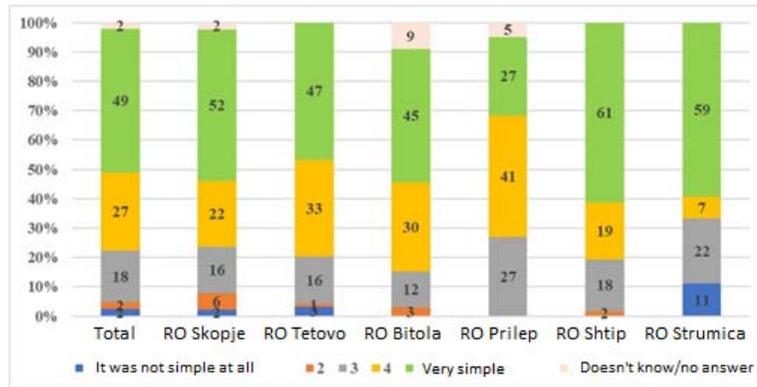
Result: Most of the respondents (39%) are generally uninformed or they have not provided answers. The percentage of generally uninformed respondents is the highest in RO Tetovo, while the percentage of respondents who are not familiar with the spending of the funds is the highest in RO Strumica.

Question: A8. Have you personally had an experience with the payment of the following taxes? - %



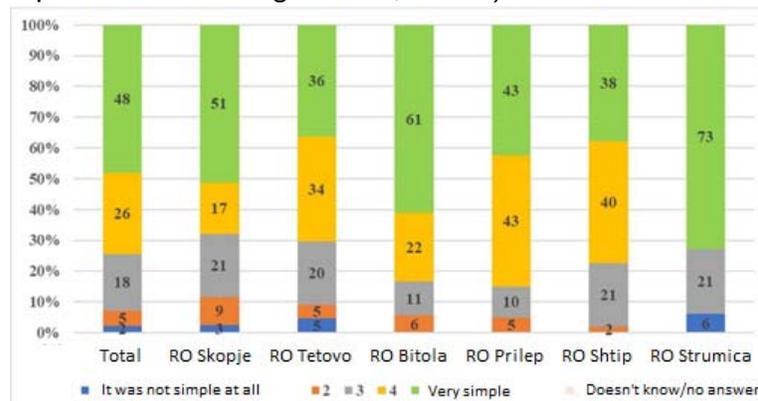
Result: The results have revealed that the citizens have personal experience mostly with paying property tax (49%), then personal income tax (34%) and inheritance tax (18 %). The percentage of respondents who have had personal experience with transfer tax is the lowest (17%). The respondents from RO Strumica and RO Prilep have mostly had experience with property tax, while those from RO Tetovo have dealt the most with personal income tax.

Question: A9. How simple was the procedure for paying personal income tax on a scale of 1 to 5 where 1 means –It was not simple at all and 5– Very simple. - % (Individuals who have had experience with the given tax, n=341)



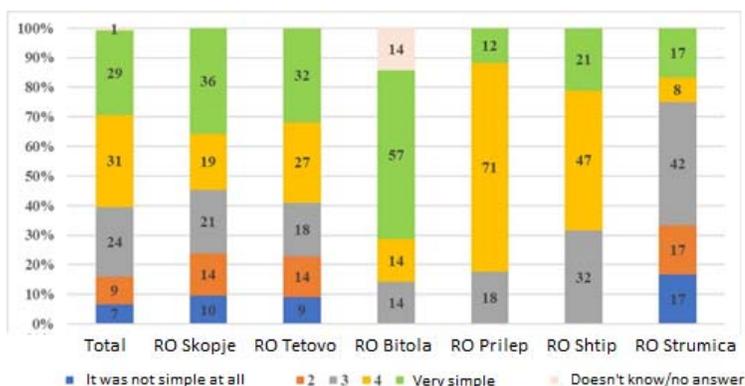
Result: The results have revealed that a very small percentage of respondents (4%) think that the payment procedure was not simple (1+2). A majority of those who think that the procedure was not simple come from RO Skopje and RO Strumica.

Question: A9. How simple was the property tax payment procedure on a scale of 1 to 5 where 1 means – Not simple at all and 5– Very simple. - % (Individuals who have had experience with the given tax, n=266)



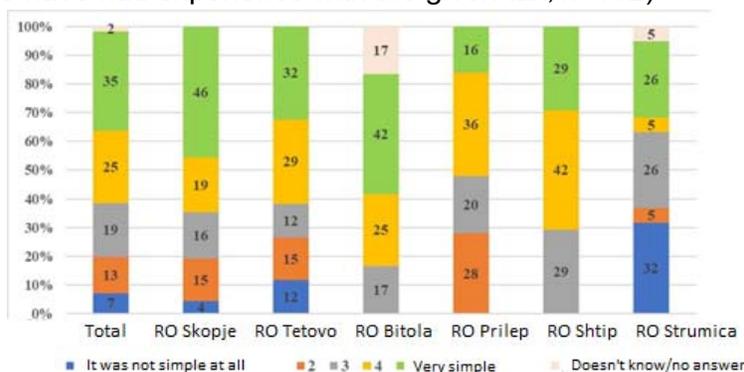
Result: The data has revealed that 7% of the respondents think that the payment procedure was not simple (1+2). A majority of them are from RO Skopje and RO Tetovo.

Question: A9. How simple was the payment procedure for real estate transfer tax on a scale of 1 to 5 where 1 means – Not simple at all and 5– Very simple. - % (Individuals who have dealt with the particular tax, n=119)



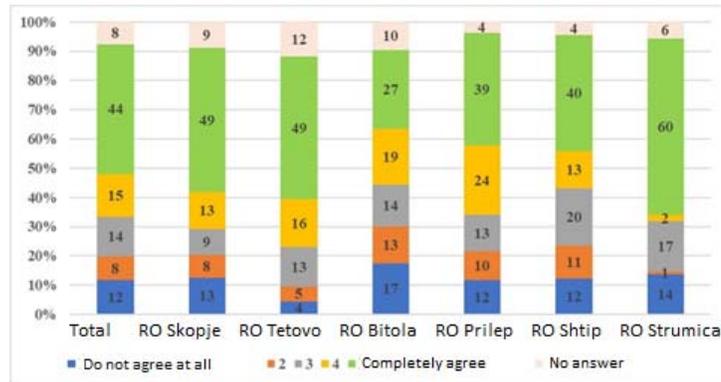
Result: As the chart demonstrates, 16% of the respondents think that the payment procedure was not simple (1+2). A majority of those who stated that the procedure was not simple come from RO Strumica, RO Skopje and RO Tetovo.

Question: A9. How simple was the procedure for gift and inheritance tax payment on a scale of 1 to 5 where 1 means – Not simple at all and 5– Very simple. - % (Individuals who have had experience with the given tax, n=182)



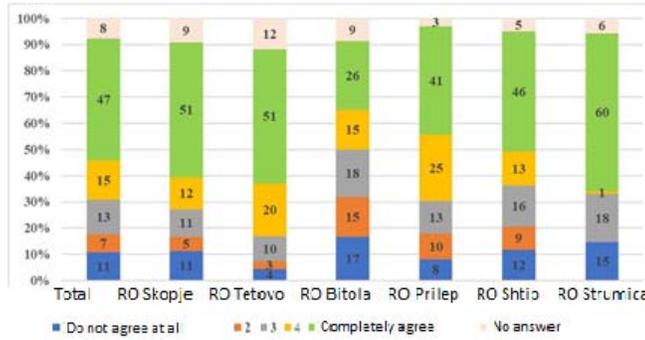
Result: One fifth (20%) of the respondents think that the payment procedure was not simple (1+2). This is mostly the case with respondents from RO Strumica, RO Prilep and RO Tetovo.

Question: On a scale of 1 to 5, where 1 means "I fully disagree" and 5 means "I fully agree", please answer to what extent you agree or disagree with A10. I am familiar with the amount of tax I have to pay. - %



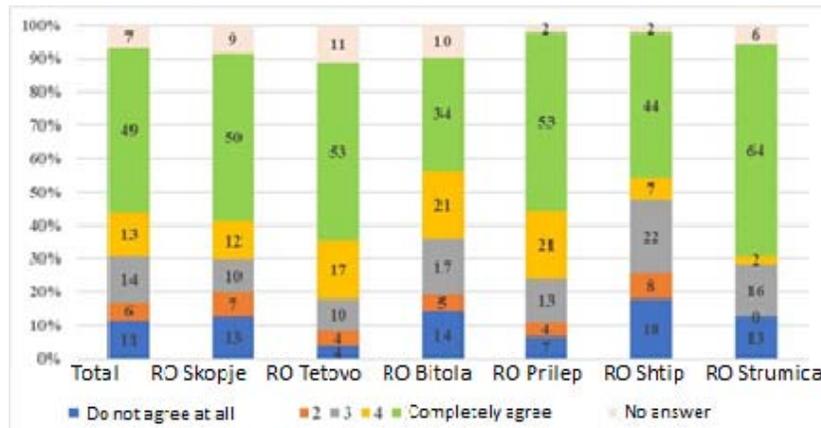
Result: 59% of the respondents stated (4+5) that they know how much they should pay as taxes. Respondents from RO Tetovo, RO Skopje, RO Prilep and RO Strumica are the ones who agree with this statement the most.

Question: On a scale of 1 to 5, where 1 means "I fully disagree" and 5 means "I fully agree", please give your answer A11. I am familiar with the type of taxes I have to pay. - %



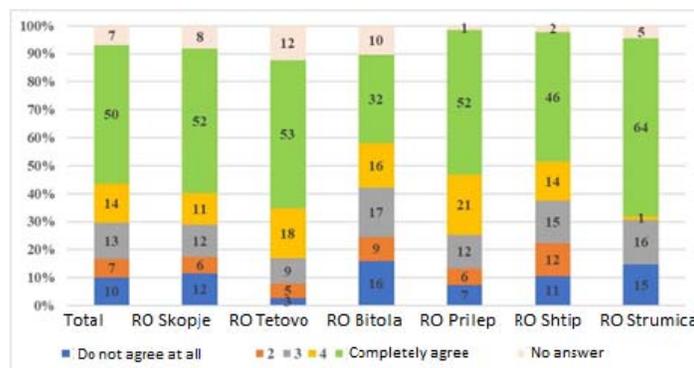
Result: As the chart reveals, 62 % of the respondents agree (4+5) that they are familiar with the types of taxes they have to pay. This percentage is the highest among respondents from RO Tetovo and RO Prilep.

Question: On a scale of 1 to 5, where 1 means "I fully disagree" and 5 means "I fully agree", please give your answer about A12. I am aware about the location where I can pay my taxes. - %



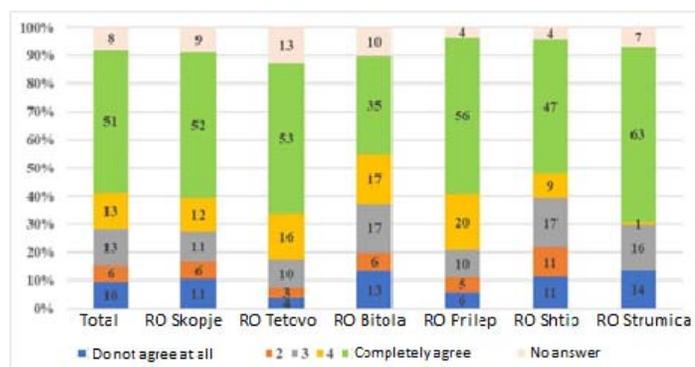
Result: The data has revealed that 62 % of the respondents agree (4+5) that they are aware about the location where they can pay their taxes. This percentage is the highest among the respondents from RO Tetovo and RO Prilep.

Question: On a scale of 1 to 5, where 1 means "I fully disagree" and 5 means "I fully agree", please provide your answer about A13. I am familiar with the ways of paying my taxes. - %



Result: Two thirds of the respondents (64%) agree (4+5) that they are familiar with the ways of paying their taxes. Most of the respondents come from RO Tetovo and RO Prilep.

Question: On a scale of 1 to 5, where 1 means "I fully disagree" and 5 means "I fully agree", please provide your answer about A14. I am aware of the deadlines for paying taxes. - %



Result: Regarding the deadlines for tax payment, 64 % of the respondents agree with the statement that they are aware of the deadlines for paying taxes. Similar to other statements, a majority of the respondents are from RO Tetovo and RO Prilep.

Question: A15. How important is it to you as a taxpayer that the tax authorities provide the following services so as to help the taxpayers? Please, provide your answer on a scale of 1 to 5 where 1 means that it is not important at all, and 5 means that it is very important. – Average

Services	Total	RO Skopje	RO Tetovo	RO Bitola	RO Prilep	RO Shtip	RO Strumica
15-1. Electronic fill-in process	3.8	3.9	4.1	3.9	3.3	3.7	3.4
15-2. Web-page	3.7	3.9	4.1	3.3	3.2	3.9	3.0
15-3. Hotline	4.2	4.3	4.6	3.9	4.0	3.8	4.6
15-4. Local offices	4.3	4.2	4.6	4.0	4.1	4.5	4.9
15-5. Direct e-mail	3.7	3.9	4.2	3.7	3.0	3.5	3.1
15-6. Community-based tax clinics	3.6	3.7	4.1	3.6	2.6	3.6	3.8
15-7. Mobile tax application	3.7	3.9	3.9	3.8	3.0	3.4	3.7
15-8. Booth-located computer terminal	3.2	3.3	4.1	3.4	2.2	3.1	3.0
15-9. Tax return on social media	3.1	3.2	3.6	3.4	2.9	2.8	2.9

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Result: The table reveals that what the citizens find the most important (the highest average value) is local offices and hotlines, while the least important services are booth-located computer terminals and tax return on the social media. Local offices were assigned the highest value in all ROs (except for the RO Skopje where the highest value was assigned to hotline services). On the other hand, the lowest value was assigned to the tax return on the social media in almost all ROs (except for RO Bitola and RO Prilep). In RO Bitola, the lowest value was assigned to the web-page service, while in RO Prilep the lowest value was assigned to the computer terminal service.

Personal Opinions about Tax System Perception, as well as the Perception of Oneself as a Taxpayer (fair treatment, morale, social norms etc.)

Question: On a scale of 1 to 5, where 1 means "I fully disagree" and 5 means "I fully agree", please provide an answer as to the extent to which you agree or disagree A16-A33. – Average

Statements	Total	RO Skopje	RO Tetovo	RO Bitola	RO Prilep	RO Shtip	RO Strumica
A16. The tax system in the country is not fair	3.6	3.7	3.8	4.0	3.4	3.4	3.3
A17. The tax system in the country is unclear	3.2	3.3	3.3	3.3	3.2	3.3	2.9
A18. If I knew more about the spending of the tax revenues, I would be always paying my taxes	3.7	3.9	4.0	3.7	3.8	2.6	4.6

A19. If I had more information about the ways, the location and the deadlines for paying taxes, I would be always paying my taxes	3.6	3.8	3.9	3.6	3.5	2.5	4.7
A20. I consider myself as a person who has always FULLY paid one's taxes	4.4	4.3	4.5	4.1	4.4	4.4	4.9
A21. I consider myself as a person who has always paid taxes within the DEADLINES	4.3	4.1	4.5	4.1	4.3	4.4	4.9
A22. Citizens have to pay their taxes so that the government can invest in their better wellbeing	4.3	4.3	4.3	4.0	4.4	4.4	4.8
A23. Taxes have to be paid because the operations of the institutions depend on it	4.3	4.3	4.3	3.8	4.4	4.4	4.7

A24. Avoiding tax payment is justifiable because the tax rates are too high	2.5	2.3	3.2	2.9	2.7	2.2	2.1
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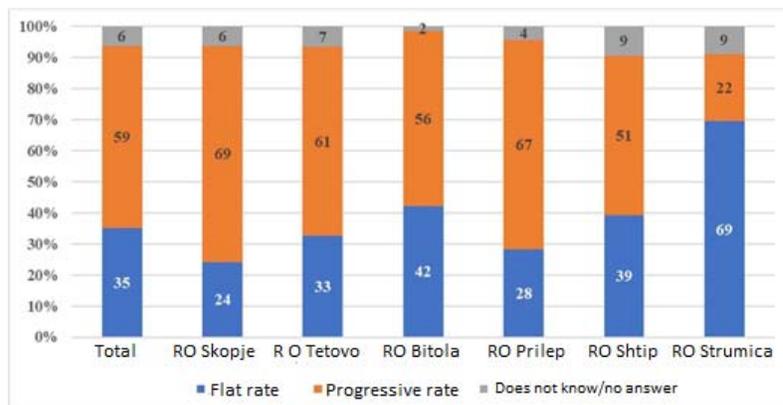
A25. I do not mind if some of my close friends or family members avoid taxes	2.7	3.0	3.3	3.1	2.5	2.0	1.9
A26. If tax revenues are not spent for citizens' needs, it is justifiable to avoid taxes.	2.8	2.7	3.3	3.3	2.9	2.4	2.3
A27. I avoid buying goods and services in the shadow economy for which no taxes are paid	2.6	2.6	2.7	2.9	3.4	2.2	2.1
A28. Avoiding tax payment is acceptable provided that the chances of being caught are minor	2.0	1.8	2.2	2.6	1.9	2.1	1.4
Statements	Total	RO	RO	RO	RO	RO	RO

		Skopje	Tetovo	Bitola	Prilep	Shtip	Strumica
A29. Tax avoidance is good provided that one has good political ties	1.7	1.6	2.1	2.2	1.7	1.6	1.3
A30. Individuals who cannot provide income for covering their costs, should avoid paying taxes whenever possible.	2.7	2.4	3.3	3.4	2.3	2.4	2.2
A31. Avoiding taxes is acceptable provided that the sanctions for failure to pay are lenient.	2.0	1.6	2.4	2.5	1.9	2.0	1.4

A32. Avoiding taxes is acceptable in case when the government is corrupt	2.6	2.4	2.6	3.3	3.2	2.2	1.9
A33. If the circumstances allow for it, I consider tax fraud as acceptable	1.7	1.5	2.1	2.3	1.7	1.5	1.2

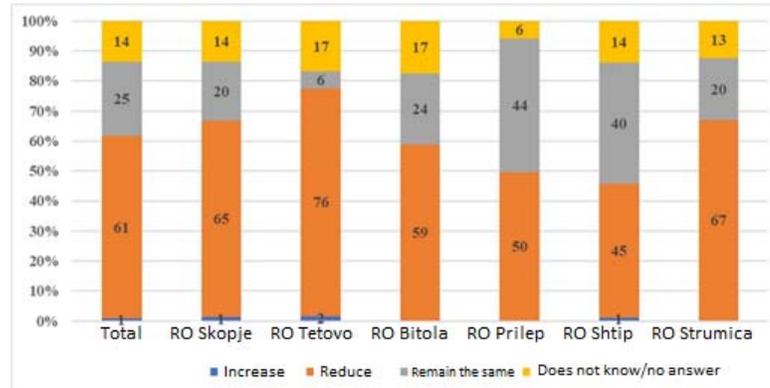
Result: It can be seen from the table that the citizens identify the most (recognize the highest average value) with the statement that they consider themselves as “individuals who have always fully paid their taxes”. On the other hand, the statements “fraud is acceptable if there is a chance for it” and “avoiding taxes is acceptable provided that one has good political ties” have received the lowest average value. The respondents from all the ROs have given the statement “individuals who have always fully paid their taxes” the highest score. On the other hand, the statement “tax fraud is acceptable if the circumstances allow for it” is a statement which is ranked the lowest in all the regions except for RO Bitola, where the lowest scored statement was that “avoiding taxes is acceptable provided that one has good political ties”.

Question: A34. In your opinion, what type of tax is a good option for income taxation?
- %



Result: Most of the respondents (59%) are in favor of progressive tax. Most of the respondents in RO Skopje and RO Prilep are in favor of progressive tax rate, while those from RO Strumica are in favor of flat tax rate.

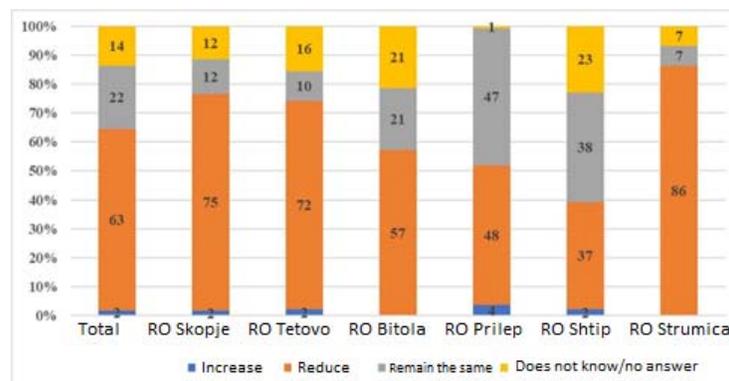
Question: A35. Do you personally think that a correction to personal income tax rate is required? - %



Result: As the chart demonstrates, a majority of the respondents (61%) think that the personal income tax rate should be reduced. Most of those respondents are from RO Tetovo, RO Skopje and RO Strumica.

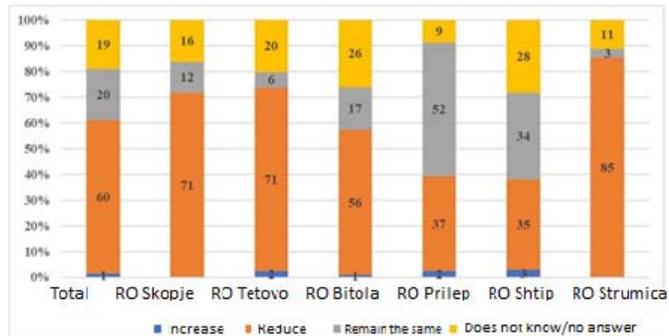
Statements on Tax Rates

Question: A35. Do you personally think that there is a need for changing the property tax rate? - %



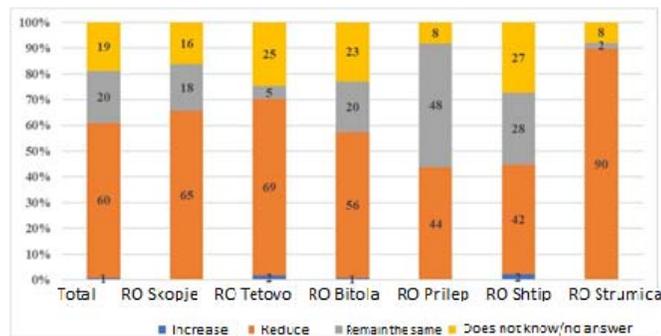
Result: The data has depicted that a majority of the respondents (63%) think that the property tax rate should be reduced. Most of the respondents come from RO Strumica, RO Tetovo and RO Skopje.

Question: A35. Do you personally think that there is a need for alterations to the real estate transfer tax rate? - %



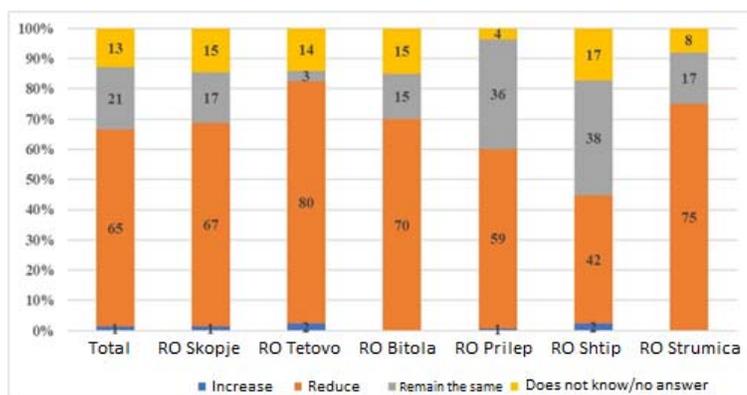
Result: Most of the respondents (60%) think that there is a need for reducing the real estate transfer tax rate. Similar to other questions, most of the respondents come from RO Strumica, RO Tetovo and RO Skopje.

Question: A35. Do you personally think that there is a need for altering the gift and inheritance tax rate? - %



Result: The results reveal that a majority of the respondents (60%) think that there is a need for reducing the gift and inheritance tax rate. Most of the respondents come from RO Strumica, RO Skopje and RO Tetovo.

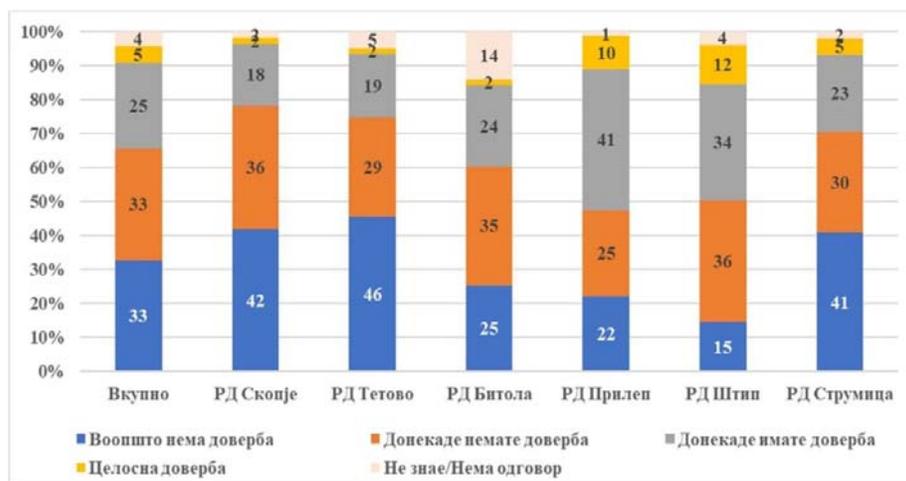
Question: A35. Do you personally think that there is a need for changing the value added tax rate? - %



Result: Two thirds of the respondents (65%) think that the value added tax rate should be reduced and a majority of them come from RO Tetovo and RO Strumica.

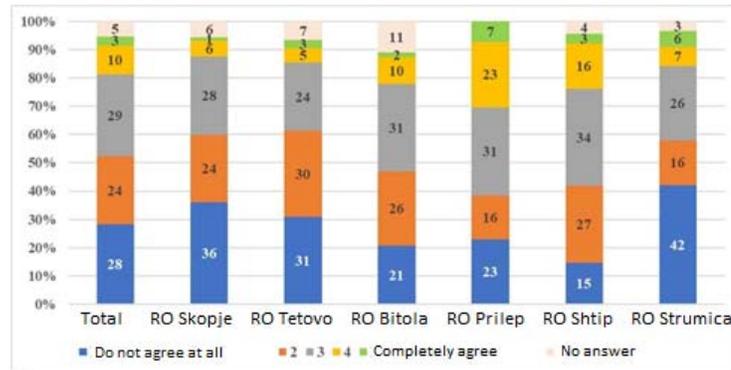
Statements about the Trust in the Institutions and the System

Question: A36. Do you personally trust the process of spending tax revenues by the local self-government (municipality), i.e. whether you fully trust, somewhat trust, somewhat distrust or completely distrust the process?? - %



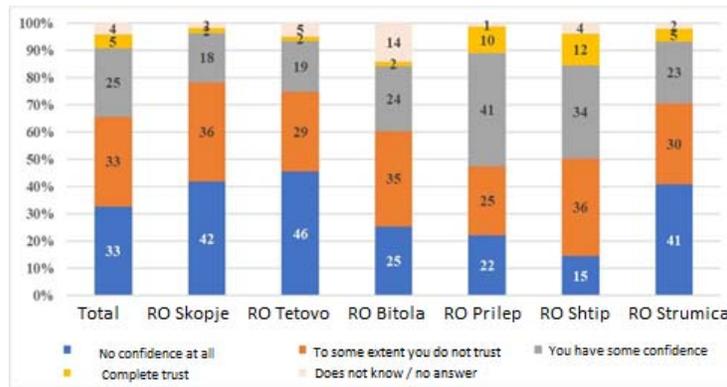
Result: According to the results, 66% of the respondents stated that they do not trust (Completely distrust or Somewhat distrust) the process of spending tax revenues by the local self-government (the municipality). These statements are mostly prevalent in RO Skopje, RO Tetovo and RO Strumica.

Question: A37. On a scale of one 1 to 5, where 1 means "I fully disagree" and 5 means "I fully agree", please rate your degree of agreement with the following statement: The revenues collected through taxes by the local self-government are well-spent on public services which are provided at local level. - %



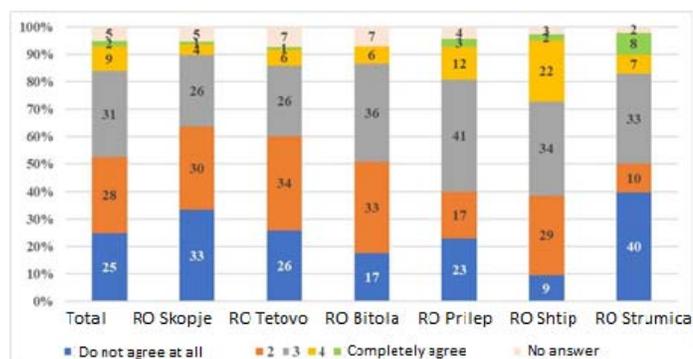
Result: The results reveal that only 13% of the respondents agree (4+5) that the tax-collected revenues by the local self-government are well spent on public services at local level. Most of the respondents who share this view come from RO Prilep and RO Shtip.

Question: A38. Please, let us know your level of trust in the Government for spending tax revenues, i.e. do you fully trust, somewhat trust, somewhat distrust or completely distrust it? - %



Result: The data has revealed that 66% of the respondents stated that they do not trust (Completely distrust and Somewhat distrust) the process of spending tax revenues by the Government (central government). Most of the respondents come from RO Skopje, RO Tetovo and RO Bitola.

Question: A39. On a scale of 1 to 5, where 1 means " I do not agree at all" and 5 means "I fully agree", please rate your answer as to the degree of agreement with the following statement: Tax revenues collected by the central government are well spent on public services provided by the central government. - %



Result: The results demonstrate that 11% of the respondents agree (4+5) that the tax revenues collected centrally are well invested into public services provided at central level. Most of the respondents come from RO Prilep, RO Shtip and RO Strumica.

Question: A40. What is your personal opinion about the priority areas of the municipal authorities for investment of the local tax revenues? PLEASE, DO NOT READ THE ANSWERS -More than one answer is possible. - %

Areas	Total	RO Skopje	RO Tetovo	RO Bitola	RO Prilep	RO Shtip	RO Strumica
Utility services and infrastructure	44	40	37	38	67	39	52
Local economic development	40	25	28	52	53	58	40
Roads	39	45	52	24	47	31	18
Education	37	61	38	19	44	17	11
Employment prospects	33	37	20	45	28	41	20
Social protection	29	29	18	31	24	46	17
Urban planning (Planning, monitoring and construction control, DUP)	24	28	24	10	21	27	36
Sports	21	32	16	17	17	20	5
Culture	18	31	13	13	14	13	6
Local administration salaries	10	15	4	10	13	9	3
Investments are good, just as before	2	2	2	2	1	4	1
Healthcare	2	1	2		2	3	2
I don't know /no answer	2	3	2	1	1		1
In line with municipal needs	1	1	2		1		
Kindergartens	1	2				1	

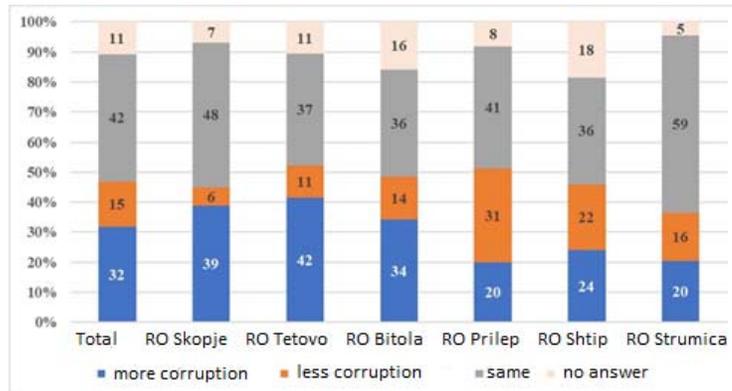
Result: Regarding priority areas for investing the local tax revenues, a majority of the respondents have listed the following: utility services and infrastructure (44%), local economic development (40%) and roads (39%). In RO Skopje, education was singled out as a major priority (61%), while in RO Tetovo roads were considered as a top priority. RO Bitola and RO Shtip put emphasis on local economic development, while RO Prilep and RO Strumica on utility services and infrastructure.

Question: A41. What do you personally think the Government should take as a priority area for investing the central tax revenues? PLEASE, DO NOT READ THE ANSWERS – More than one answer is possible. - %

Areas	Total	RO Skopje	RO Tetovo	RO Bitola	RO Prilep	RO Shtip	RO Strumica
Healthcare	72	77	78	63	73	68	61
Roads and other capital investments	56	48	52	57	77	62	49
Education	47	60	34	32	62	42	40
Employment prospects	45	47	33	52	44	46	50
Social protection	38	35	20	48	42	45	49
Sports	25	34	18	21	24	21	20
Culture	25	43	16	12	21	16	26
Public administration salaries	16	21	9	21	8	16	16
Well invested, just as before	2	1	2	2	2	6	1
I don't know / no answer	2	3	1	1	2		1
Need-based	1		4		1		
All areas	1		1			3	1
Balanced regional development	1		3				

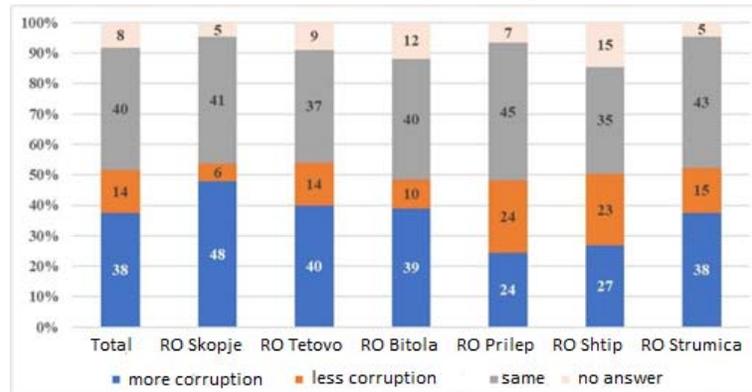
Result: Regarding the government priorities, a majority of the respondents (72%) think that healthcare should be a priority of the government for investing the central tax revenues. Healthcare was seen as a priority in all the RO, except for RO Prilep where it was ranked second, right after roads and other capital investments which were seen as a priority.

Question: A42. Do you think that the present corruption level is higher or lower compared to the period of 5 years ago? - %



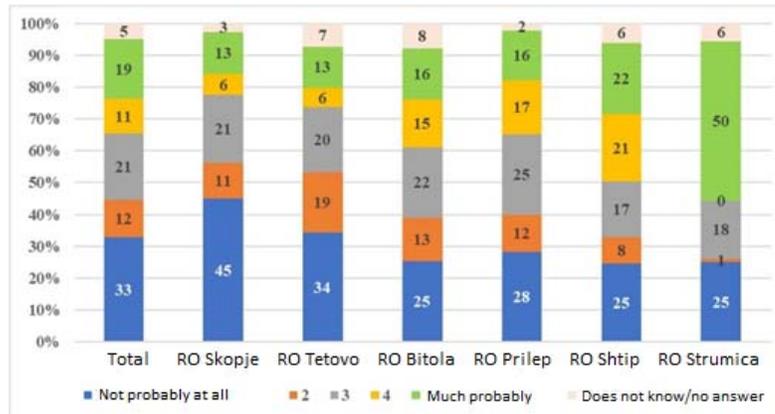
Result: Regarding corruption, most of the respondents (42%) think that the level of corruption in their municipality has remained unaltered compared to the period from 5 years ago. RO Tetovo has a higher percent of respondents who think that the current level of corruption is higher, rather than being unaltered.

Question: A43. Do you think that the present corruption level in the Government is higher or lower compared to the period from 5 years ago? - %



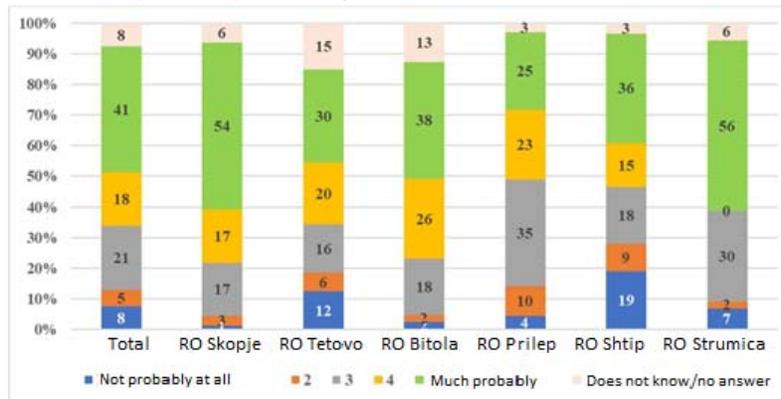
Result: Regarding corruption, the respondents are divided, i.e. 40% think that the level of corruption in the government has remained unaltered, while 38% think that the level of corruption is higher compared to the period 5 years ago. RO Strumica, RO Bitola, RO Prilep and RO Shtip have marked higher percentage of respondents who think that the corruption level has remained unaltered, while RO Tetovo and RO Skopje has more respondents who think that the corruption level is higher now.

Question: A44. If I pay higher taxes, I would receive better services. On a scale of 1 to 5, where 1 means "Highly unlikely" and 5 means "Highly likely", please rate the following statement. - %



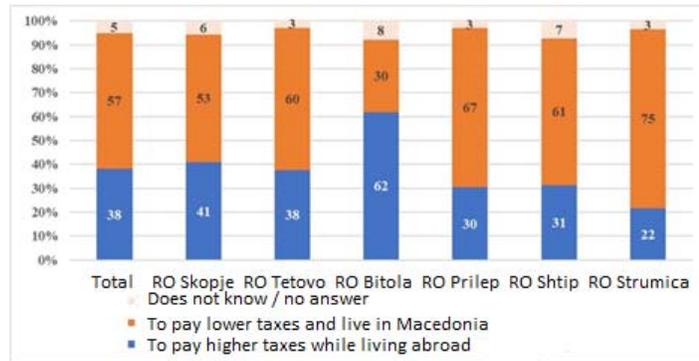
Result: According to the results, about one third (30%) of the respondents think that if they were to pay higher taxes, the probability (4+5) is that they would also get better quality services. This is mostly prevalent in RO Strumica, where almost half of the respondents consider it highly probable.

Question: A45. If I pay higher taxes, it only means that more money will be misused by the authorities. On a scale of 1 to 5, where 1 means "not probable at all" and 5 means "very probable", please provide your answer about the statement. - %



Result: The chart reveals that 59 % of the respondents think that, if they pay higher taxes, it is probable (4+5) that more money will be misused by the authorities. This opinion is very prevalent in RO Skopje and RO Bitola.

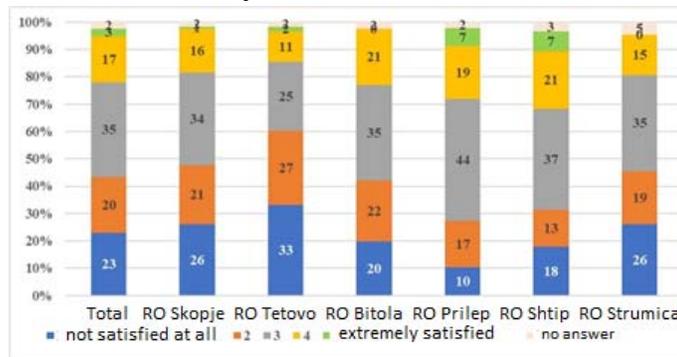
Question: A46. Would you rather: - %



Result: The results reveal that a majority of the respondents (57%) would like to live in Macedonia and pay lower taxes. This refers to the respondents from RO Skopje, RO Tetovo, RO Prilep, RO Shtip and RO Strumica, while the respondents in RO Bitola have a different opinion, i.e. they would rather live abroad and pay higher taxes.

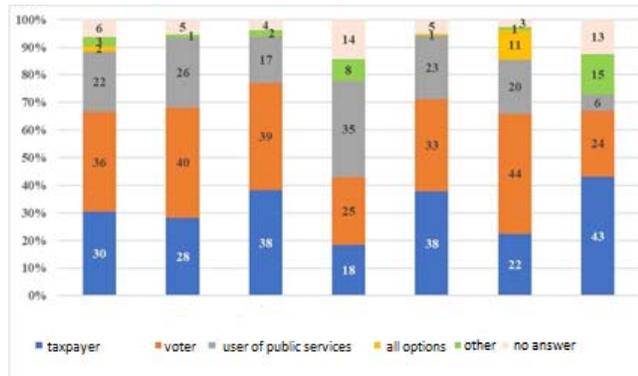
Attitudes about Democracy

Question: A47. On a scale of 1 to 5, where 1 means "not satisfied at all" and 5 means "very satisfied", please provide your answer on how satisfied you are with the democracy system in the country? - %



Result: Most of the respondents (43%) are not satisfied (1+2) with the democracy system in the country. Most of the dissatisfied respondents come from RO Tetovo and RO Skopje.

Question: A48. If you were to choose one option, what type of a treatment do you feel that you receive and how do you perceive yourself: - %

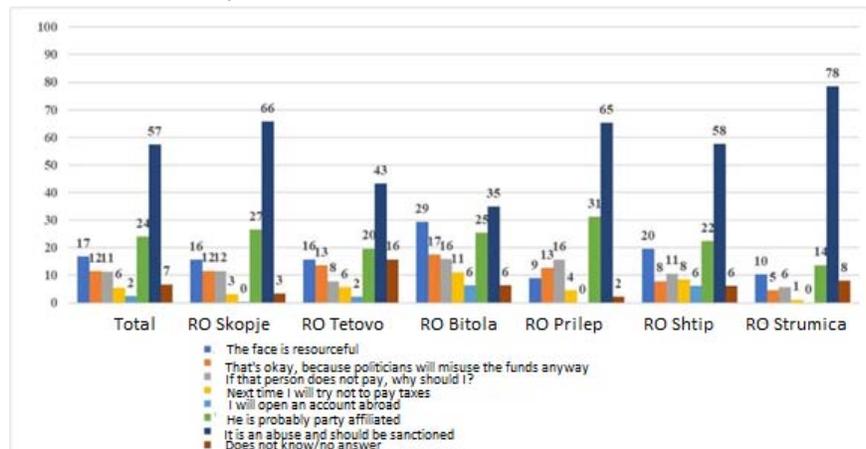


Result: Regarding the treatment, 36 % of the respondents perceive themselves as voters. This feeling is very prevalent in RO Skopje, RO Tetovo and RO Shtip. 30 % of the respondents perceive themselves as taxpayers, and this is mostly prevalent in RO Prilep and RO Strumica.

Attitude towards Tax Morale as a Social Norm

Question: A49. What is your opinion about an individual who does not pay taxes?

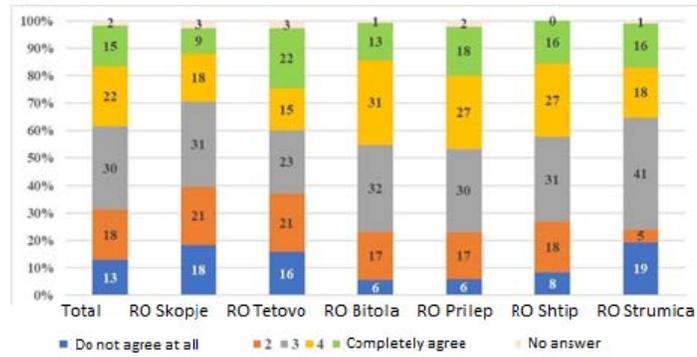
– More than one answer is possible - %



Result: Regarding individuals who do not pay taxes, most of the respondents (57%) think that it is a misuse and has to be sanctioned (in all the ROs). For 24% of the respondents, political ties play a role (second answer in all the ROs).

Attitude towards Work

Question: A50. On a scale of 1 to 5, where 1 means "I fully disagree" and 5 means "I fully agree", please provide an answer about the following statement: In the long run, hard work will bring better life and success. - %



Result: Only 37% of the respondents agree (4+5) with the statement that on the long run, hard work will certainly bring better life and success. Most of the respondents who agree with the statement come from RO Bitola, RO Prilep and RO Shtip, while RO Skopje marks the lowest number of respondents.

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