INTRODUCTION

Curbing corruption in the tax administration is closely related both to the overall reform of the public administration and to the prevention of shadow-economy practices and in particular, tax fraud and other tax offences. Having a more effective public administration and less corruption is among the main challenges facing Bulgaria on the last stretch of its road to EU accession. EU Member States are particularly sensitive to tax fraud, which, after the country's accession, and especially in the VAT area, will pose a threat to the Union's, as well as to Bulgaria's, interests.

The 2000 Lisbon Agenda has raised additional challenges to the quality of the tax and regulatory environment to ensure more cost-competitive products. Reducing the tax burden and the scope of the shadow economy are among the top medium-term priorities of government today. Success in these areas depends, among other things, on higher collection and voluntary compliance rates. Overall, the effectiveness of lowering taxes by raising collection rates is a function of curbing tax-related corruption.

Tax-related corruption largely determines the levels of all other kinds of corruption. If they did not underreport sales and keep two sets of cashbooks to evade taxes, businesses would not have the corruption money that changes hands in public procurement or in the various licensing or permitting procedures, or in the delivery of public services or even in business-to-business dealings. Consequently, curbing tax corruption would have the effect of curbing all other kinds of corruption by cutting their 'supply lines'.

However, despite their considerable public significance, a number of questions concerning the factors and mechanisms of the corrupt environment and practices in the tax administration remain unanswered. Studies of this problem area rely mostly on surveys among taxpayers. Given that most researchers focus on the breadth and depth of corruption, such one-sidedness is understandable. In this regard, taxpayers' opinion is more important—not because it is necessarily more accurate but because corruption is an important component and indicator of the business environment. Economic agents make their investment decisions on the strength of perceptions, regardless of how close to reality they are. Therefore, as *a stumbling block to investment*, corruption is best seen with the eyes of the public.

If however, the purpose of a study is to analyse the relative weight of tax-related corruption factors and drivers, and recommend countermeasures on that basis, taxpayers' perceptions are not enough: corruption must be analysed from the perspective of business, i.e., the demand side, but also, from its supply side, i.e., from the perspective of the administration. Moreover, any corruption prevention measures recommended without regard to the taxman's opinion would be largely doomed to failure. It is all the more surprising then that almost no such surveys of the Bulgarian tax administration have ever been conducted.

This study is an attempt at an in-depth diagnosis of tax-related corruption in terms of its drivers at work in individual and institutional behaviour. To assess the problem's

scale, we have relied on information from business and members of the public, from the Corruption Monitoring System (CMS) run by *Coalition 2000* and from various other Bulgarian sources. We have also shown the corruption ratings of the Bulgarian tax administration according to various international indices. In addition, specially for the purposes of this study, we have conducted a survey among Bulgarian tax officers, which has allowed an analysis of individual motives and institutional factors on the supply side of corrupt services. While the survey does shed some light on the size and incidence of corrupt transactions, its value lies in the information about the regulatory and management mechanisms and deficiencies which make corruption possible in the first place.

Chapter One outlines the conceptual framework of the study's positive and normative analysis. It sets the objectives of the policy impact on the basis of a transactional typology of the acts of corruption in the tax administration, i.e., in the context of the supply and demand of certain services. Then, the identification of drivers on the supply side and on the demand side of corruption allows a more accurate targeting of policy measures and the monitoring and evaluation of impacts. *Chapter Two* presents an attempt at determining the depth and dynamics of the problem in terms of the various corruption indicators, including the spread of corruption by administrative level and functional unit. *Chapter Three* is an analysis of the techniques and mechanisms of corrupt transactions in the tax administration. The distinction is made between corruption seeking a better quality of service and corruption as an inducement to commit or to cover up at tax offence. Described in this chapter are also the concrete individual motives and institutional factors which drive the administration's corrupt behaviour. In addition, *Chapter Four* dwells particularly on the tax administration's greatest challenge–VAT fraud–describing its various types and mechanisms, including an evaluation of the VAT account arrangement. Based on the above, *Chapter Five* presents the main policy priorities with a view to curbing corruption in the tax administration. Two main groups of measures have been identified: 1. incentives; and 2. ways of eliminating the legal and institutional factors which invite tax corruption. Section 3 of this chapter dwells in particular on measures against VAT fraud. *Chapter Six* proposes a set of indicators to monitor and evaluate progress in the fight against corruption in the tax administration. The main conclusions and policy guidelines are briefly summarised at the end.

The above notwithstanding, the views and conclusions presented here may not be attributed to any of these individuals in particular, or to the institutions for which they work. The author is solely responsible for any misinterpretation or omission.