

Audit Hierarchy in a Corrupt Tax Administration

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Bribe chains arise when a hierarchy of corruptible auditors audits taxpayers.

We investigate reward structures for inducing truth-revealing equilibria with no bribes. We show that if auditors are rewarded for detecting tax evasion, then no super-auditing is necessary for income revelation in a one-off audit. However, such equilibria do not survive repeated encounters, even with super-audits.

We then show that if rewards depend on tax collection, then truth-revealing equilibria can be sustained over repeated encounters. In such structures, the number of levels in the hierarchy is immaterial for truth revealing, but it determines the net revenue of the government.

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