

UNDERSTANDING SOCIAL NETWORKS CAN HELP TACKLE TAX EVASION

Gathering information on which taxpayers are linked to which other taxpayers gives tax authorities the ability to target audits more effectively, according to research by **Duccio Gamannossi degl'Innocenti** and **Matthew Rablen**.

Their study, to be presented at the annual congress of the European Economic Association in Manchester in August 2019, analyses the value of a new HMRC system called *Connect*, which cross-checks public sector and third-party information, seeking to detect relationships among people and organisations.

Researchers have analysed the role of social networks in explaining levels and patterns in tax evasion behaviour, and how tax authorities like the UK's HMRC can potentially exploit their knowledge of social networks to improve the targeting of their tax audits. There are strong initial returns to using a small amount of social network information to target audits.

There is a long-held belief that the tax evasion decision is not a purely private decision, but rather also reflects prevailing social norms towards tax compliance. Taxpayers may also share information about their own experiences with each other, allowing for the spread of evasion techniques (such as evading VAT through cash payments), and for the spread of evidence as to the likelihood that particular acts of evasion will be investigated by the tax authority.

Moreover, to the extent that people tend to compare their standard of living to other people around them, tax evasion may be route used by some to try and 'keep up with the Joneses'.

Tax authorities have long had an interest in understanding social networks, in the hope of being able to manipulate the social norm for tax compliance, or to predict patterns in evasion that help to target tax audits at evaders. While these intentions may in the past have been little more than a pipe dream, the advent of 'big data' is making it possible for tax authorities to at least partially construct social networks.

HMRC has a system called *Connect*, which crosschecks public sector and third-party information, seeking to detect relationships among people and organisations. The system produces 'spider diagrams' linking individuals to other individuals and to legal entities such as property addresses, companies, partnerships and trusts.

Researchers [Duccio Gamannossi Degl'Innocenti \(Catholic University of Milan\)](#) and [Matthew Rablen \(University of Sheffield\)](#) analysed the improvements in audit yield from exploiting social network information. There are strong initial returns to being able to exploit a small proportion (up to 20%) of information about which taxpayers are linked to which other taxpayers. Thus, investment in technology such as *Connect* has the potential to pay off in terms of improved targeting of audits.

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Further details can be found at:

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