

ABSTRACT

THE HIDDEN ECONOMY AND TAX EVASION IN TRINIDAD AND TOBAGO

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Recent research has shown that the hidden economy in certain developing countries is more than 70% of official GDP. The purpose of this study is to estimate the size and determine the structure of the hidden economy in Trinidad and Tobago, and to deduce therefrom the extent of tax evasion in Trinidad and Tobago. The causes and consequences of the existence of the hidden economy will also be explored, as well as the underlying causes of tax evasion.

Estimation of the size of the hidden economy is carried out using both a direct method and an indirect method. The direct method applied is the survey technique. The survey was undertaken by administering a questionnaire face-to-face to a sample of households and small business owners in Trinidad and Tobago during the period October-November 2003. One questionnaire was used for households and another for small businesses. Multivariate statistical techniques (probits, multinomial logits and ordered probits) were used to determine the structure and causes of the hidden economy. The indirect method is a structural cointegrating VAR approach using Tanzi's (1980, 1982) currency demand model as a starting point in estimating a multiple equation. The system was solved using a Gauss-Siedel algorithm. The results of this exercise were then used to calculate the amount of tax evasion, and examine the relationship between tax evasion and per capita income, external debt, unemployment and inflation for the period 1970-2000.

In all cases, the size of the hidden economy as a proportion of measured GDP was calculated, and estimates made of the amount of tax evasion in Trinidad and Tobago.