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Impact of Corporate Tax Evasion by Multinational Companies on Malawian Economy: The Case Study of Mota Engil Group

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ABSTRACT

This study evaluated the impact of corporate tax evasion by multinational companies on Malawian economy: the case of Mota-Engil Group. Specifically, the study sought to achieve the following objectives; To assess the extent of tax evasion by multinational corporations in Malawi; To identify methods used by multinational corporation to evade tax; To determine the impact of corporate tax evasion of multinational corporations to Malawi Government revenue; To identify measures to control tax evasion. To conduct this research, purposive sampling technique was used and sample size 50 was adopted. Questionnaires were used as a method for data collection and Microsoft Excel and Statistical Package for the Social Science (SPSS) version 20.0 was used as data analysis method. The study reveals a significant concern among respondents regarding the extent of tax evasion by multinational corporations (MNCs) in Malawi. A majority perceive underreporting of taxable income as a frequent or ongoing issue, with many believing that MNCs fail to declare a substantial portion of their revenue for tax purposes. The scale of tax evasion by MNCs is seen as a very significant problem compared to other tax compliance issues, indicating widespread concern over its negative impact on Malawi's economy. These findings reflect broader global trends, especially in developing countries with weak tax enforcement, highlighting the urgent need for strengthened tax administration and enforcement mechanisms. The study makes the following recommendations: Strengthen transfer pricing regulations and enforcement; Assess the impact of tax incentives on revenue losses; Examine the capacity of the Malawi Revenue Authority (MRA); and increase penalties for non-compliance.

KEY WORDS: Tax Evasion- Corporate tax evasion refers to the deliberate and illegal practices by corporations to reduce their tax liabilities by concealing income, overstating expenses, or exploiting loopholes in ways that contravene the law.

Multinational corporations (MNCs) -are enterprises that own, control, or manage production and service operations across multiple countries, while maintaining strategic coordination from a central headquarters (Dunning & Lundan, 2008.

INTRODUCTION

Corporate tax evasion by multinational companies (MNCs) has emerged as a critical issue in global economic discourse, particularly in developing countries where fiscal resources are scarce and essential for socio-economic development. Tax evasion, defined as the illegal act of paying less tax than required by law, contrasts with tax avoidance, which exploits legal loopholes to minimize tax liabilities. Both practices, however, deprive governments of revenue needed to fund public services such as healthcare, education, and infrastructure. While tax avoidance operates within the boundaries of legality, it often borders on ethical ambiguity, enabling MNCs to shift profits aggressively and erode the tax bases of host nations.

In the context of Malawi, a low-income country heavily reliant on tax revenues to address poverty and underdevelopment, the impact of tax evasion by MNCs is particularly pronounced. This study focuses on the Mota-Engil Group, a Portuguese multinational corporation operating in Malawi's construction, infrastructure, and energy sectors, to examine how its tax practices affect the Malawian economy. By drawing on empirical literature, this analysis explores the global scale of corporate tax evasion, its disproportionate effects on developing countries, and the specific vulnerabilities in Malawi's economic and fiscal landscape.

LITERATURE REVIEW

The concept of corporate tax evasion

Corporate tax evasion, the deliberate and illegal act of a company paying less tax than legally mandated, stands as a formidable challenge to global economic stability and social equity. This practice, distinct from tax avoidance which exploits legal loopholes, involves fraudulent activities designed to conceal taxable income. It fundamentally undermines the social contract, as corporations benefit from public infrastructure and services funded by taxpayers but fail to contribute their fair share. As Murphy (2012) argues, tax is not only a fiscal mechanism but also an essential component of the relationship between citizens, businesses, and the state, and when corporations evade taxes, they erode the legitimacy and fairness of that relationship. Drawing from relevant literature, this discussion provides a coherent overview of the mechanisms, contextual differences, and profound consequences of corporate tax evasion.

The prevalence of corporate tax evasion varies significantly across economic contexts. Sookram and Watson (2005) found it to be particularly widespread in developing economies, where institutional capacity, tax administration, and enforcement mechanisms are often weak. This finding resonates with Bird and Zolt (2005), who argue that developing countries face systemic difficulties in enforcing tax compliance because their tax bases are narrow, and a few large enterprises dominate economic activity, making them both the most significant contributors and potential evaders. Auriol and Warlters (2005) further substantiate this disparity by highlighting that direct taxation in Sub-Saharan Africa accounts for only about 7% of GDP, compared to 22% in industrialized nations.

Theoretic Literature Review

The underground economy

The formal economy, with its regulated markets, transparent transactions, and established legal frameworks, is only one part of the economic landscape in many countries, particularly in the developing world. Alongside it operates a vast and complex parallel system known as the underground economy. Its roots and proliferation are deeply intertwined with the challenges of tax administration and compliance. The origin of formal writings on this phenomenon can be traced to 1971, when anthropologist Keith Hart, in a study on the economy of Ghana, first coined the term "informal economy" to describe the unrecorded, unregulated economic activities of urban dwellers. While initially used to characterize a survivalist response to poverty, the concept has since evolved to encompass a wide range of illicit and unrecorded activities that evade the scrutiny of tax authorities. As Tanzi and Shome (1993) observed, there has been a growing global concern about the expanding nature of these activities and their profound impact on economic policies and fiscal health. This essay will argue that the underground economy is a major driver of tax evasion and that its existence is not only facilitated by corruption and administrative weaknesses but also initiates a vicious cycle of inequity and inefficiency that undermines the entire tax system. The case of the Kenyan "Jua-kali" sector provides a poignant example of this complex dynamic.

The underground economy is not a monolithic entity but a diverse collection of activities that share one common characteristic: they are deliberately concealed from the authorities to avoid taxation, regulation, or other legal obligations. These activities range from the outright illegal, such as smuggling, counterfeiting, and the trade in prohibited goods, to the legally gray, such as informal labor or unreported cash transactions. The user’s observation that such activities are on the increase, often concealed within legitimate businesses, underscores the sophistication and resilience of this sector. The motivations for participating in the underground economy are varied, including a desire to reduce costs, avoid bureaucratic red tape, and, most prominently, to escape the tax net. Unlike the formal sector, where income and transactions are easily traceable and subject to third-party reporting, the informal economy operates largely outside the view of tax collectors, making it an ideal environment for tax evasion.

The Economics of Crime Model

The economic theory of tax evasion, rooted in Gary Becker’s seminal 1968 work on the economics of crime, provides a foundational framework for understanding tax compliance behavior. Becker’s model, originally developed to analyze criminal behavior, posits that individuals make rational decisions by weighing the benefits of committing a crime against the risks of detection and punishment, questioning whether deterring crime is always socially desirable. This rational choice approach was adapted to tax compliance by Allingham and Sandmo in 1972, marking a pivotal application of the economics of crime model to fiscal behavior. Their model assumes that a rational individual maximizes the expected utility of the tax evasion gamble, balancing the financial gains of underreporting income or overstating deductions against the potential costs of detection and penalties. This framework has dominated compliance research, emphasizing enforcement mechanisms like audits and penalties as primary determinants of tax compliance. However, empirical and theoretical critiques, supported by scholars like Osoro Nehemiah (1995), highlight that compliance cannot be fully explained by financial considerations alone, as non-economic factors such as corruption, tax morale, and social norms significantly influence taxpayer behavior.

Prospect Theory

The study of tax evasion has long been connected with economic decision-making models that assess how individuals and firms behave under conditions of risk and uncertainty. The Expected Utility Theory (EUT), first formalized by von Neumann and Morgenstern (1944), provided one of the earliest frameworks to explain choices made in risky environments. Within this framework, taxpayers are assumed to weigh the expected benefits of evading tax against the probability and magnitude of detection and punishment. This model gained traction in the 1970s and was applied extensively to questions of compliance and evasion. However, a key contribution came from Yitzhaki (1974), who applied EUT to the case of tax evasion and found a surprising prediction: if fines are proportional to evaded income, an increase in tax rates would reduce the incentive to evade taxes. This is because, under the assumption of decreasing absolute risk aversion (DARA), the relative utility loss from detection increases with higher tax rates, making evasion less attractive. This outcome—commonly referred to as the “Yitzhaki Paradox”—contradicted much of the observed empirical evidence, which often shows that higher tax rates correlate with higher levels of tax evasion.

International Political Economy of Taxation

The international political economy of taxation examines the interplay of economic, political, and institutional forces shaping tax systems in a globalized world. It focuses on how states, multinational corporations (MNCs), international organizations, and global markets interact to influence tax policies, compliance, and outcomes, particularly in the context of cross-border capital flows and trade. Taxation is not merely a fiscal tool but a political instrument that reflects power dynamics, sovereignty, and distributional conflicts. In the global arena, these dynamics are amplified by the mobility of capital, competition for investment, and disparities in state capacity, especially between developed and developing nations. The literature highlights how tax policies are shaped by global economic integration, the rise of tax havens, and international efforts to curb tax evasion and avoidance, with significant implications for equity, development, and governance.

The global tax system operates within a framework of sovereign states, yet it is deeply interconnected due to globalization. MNCs exploit this by leveraging tax havens, transfer pricing, and complex financial structures to minimize tax liabilities, often shifting profits to low-tax jurisdictions. Estimates suggest that 40% of MNC profits are shifted to tax havens, costing governments US$200-600 billion annually in revenue, with developing countries losing a disproportionate share relative to their GDP. This practice, often blending legal tax avoidance with illegal evasion, thrives in a system where national tax policies are undermined by global competition. The political economy perspective emphasizes that taxation is not just technical but a site of contestation between states seeking revenue, firms pursuing profit, and citizens demanding fairness.

Emperical Review

Global Context

The conceptual understanding of tax evasion is built upon a broad body of research that explains its motives and methods. Charles, Agnes, and Dorothy (2012) provide a seminal perspective, linking tax avoidance and evasion to "creative accounting practices" within corporations. Their study on companies in Kenya found that these illicit activities are perpetrated through a range of deceptive actions, including presenting false financial statements, making false entries or alterations, destroying records, and the concealment of assets. This framework establishes that corporate tax evasion is not merely a passive oversight but a deliberate and active strategy aimed at manipulating financial reports to reduce tax liabilities. This "creative accounting" is a direct response to the pressure to show higher profits while simultaneously paying less tax.

The global scale of corporate tax evasion is staggering, representing a profound challenge to fiscal sovereignty and equitable wealth distribution. Conservative estimates suggest that MNCs shift approximately 40% of their profits to tax havens, resulting in a revenue loss of around $650 billion annually for governments worldwide (Zucman, 2015). This lost revenue, if collected, could be transformative, particularly for countries struggling with poverty and underdevelopment. Sookram and Watson (2005) carried out a comparative study on tax evasion in developed and developing countries, concluding that evasion is more widespread in developing economies. They attributed this to several factors: these economies are often based on a few large enterprises, the population is generally less wealthy, and the general tax morale is low. While the public may have reduced opportunities for sophisticated evasion, the large firms have a greater capacity to engage in it. This observation highlights the dual challenge for governments: managing the tax compliance of a small number of powerful corporations while simultaneously fostering a culture of tax compliance among the broader populace.

African Context

Levin Amaluka’s (2001) study on tax evasion in Kenya and Tanzania offered significant insights into trade-related practices that undermined fiscal performance. Focusing on “missing imports”—goods unreported at border points—Amaluka demonstrated that tax evasion through customs fraud was a major contributor to poor tax performance, directly impeding economic growth. His analysis showed that unreported imports led to substantial losses in customs duties, a critical revenue source for both countries. Amaluka recommended investments in modern technologies, such as electronic customs systems, to deter evasion and smuggling, emphasizing the link between administrative capacity and effective tax collection. This finding aligned with Bird and Zolt (2005), who argued that developing countries’ narrow tax bases and weak enforcement mechanisms made them particularly vulnerable to trade-related evasion, a challenge highly relevant to Malawi’s landlocked economy reliant on imported goods.

RESEARCH METHODOLOGY

Research Design

A descriptive research design of a case study nature was employed in this study.

Target Population

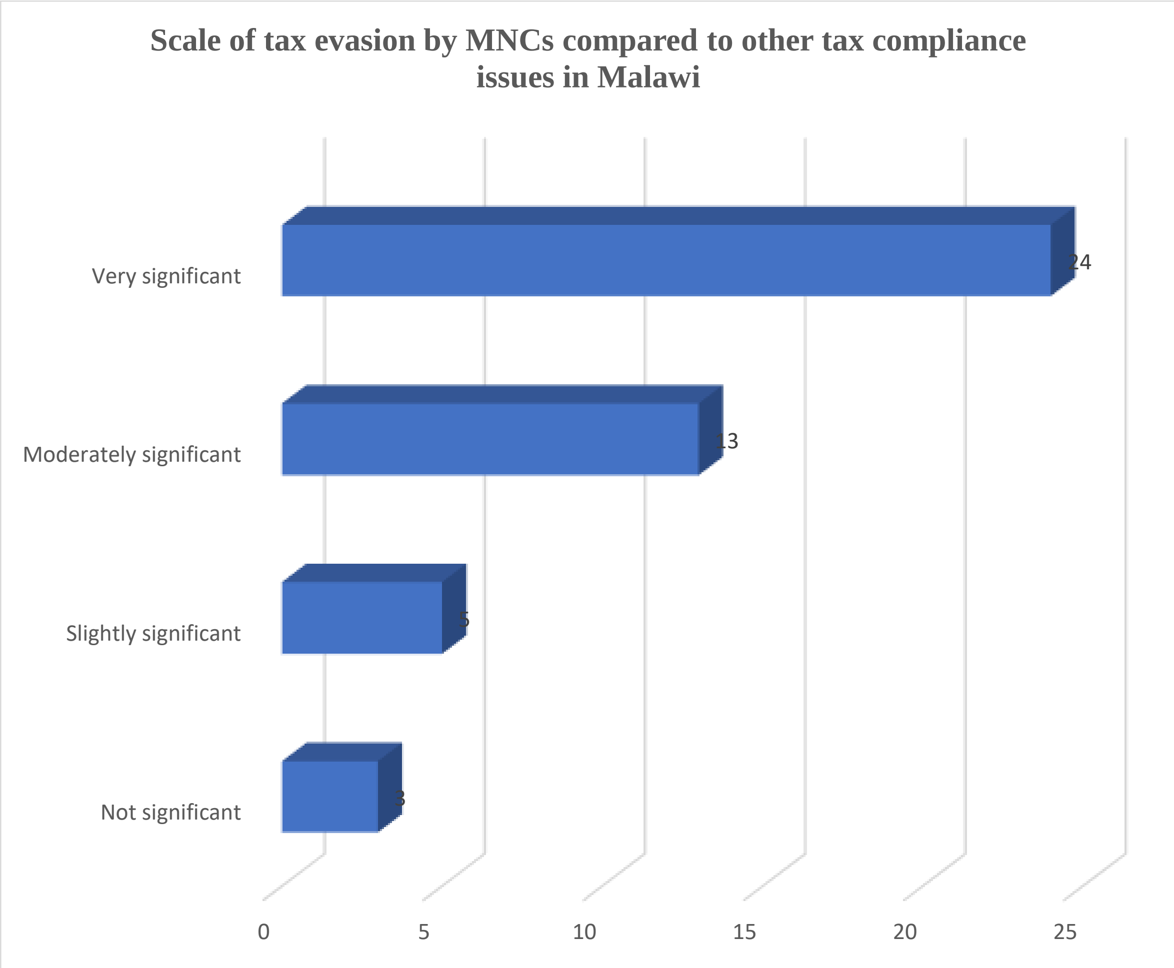
The population of this study included key stakeholders involved in corporate taxation and economic governance in Malawi, focusing on the impact of tax evasion by Mota-Engil Group. It comprises officials from the Malawi Revenue Authority (MRA) and the Ministry of Finance.

Sampling

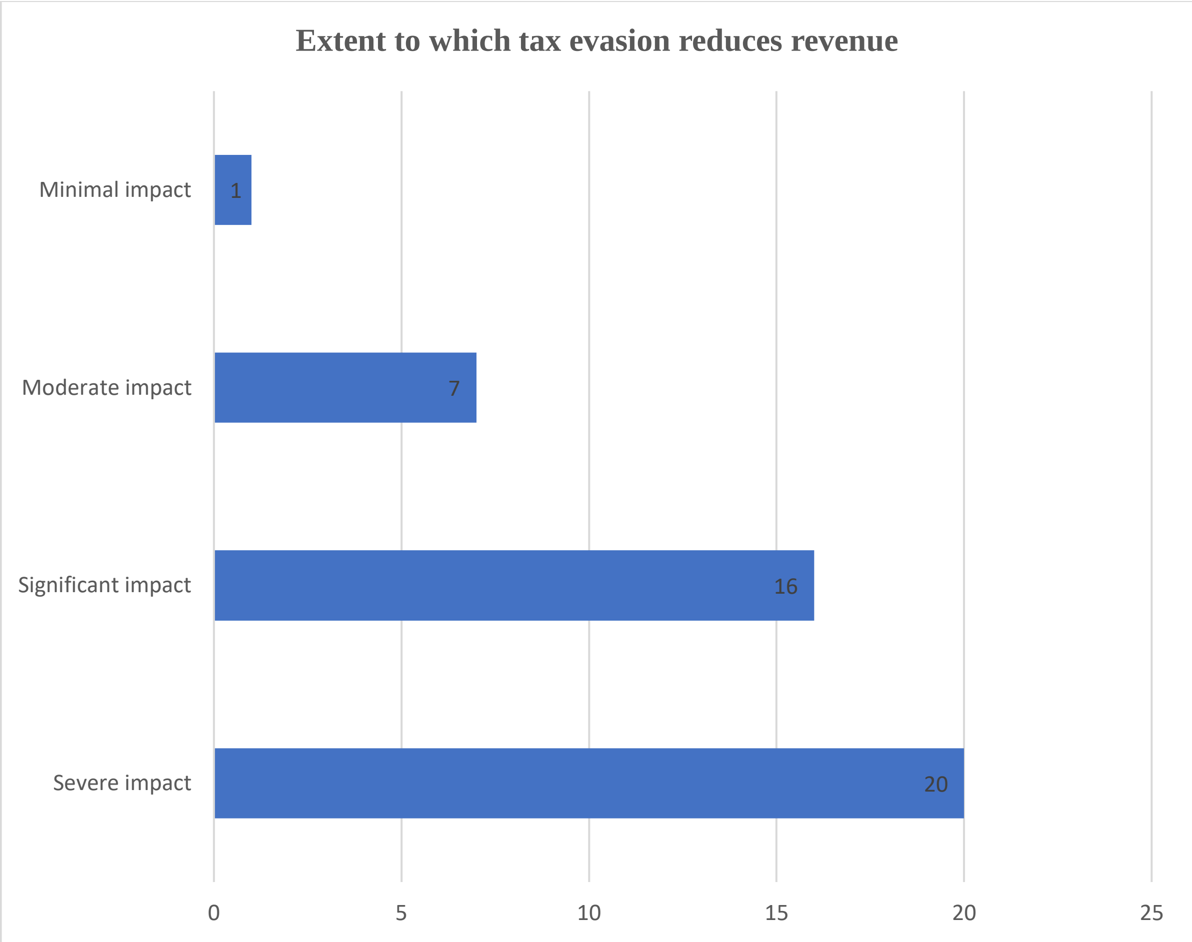
Purposive sampling was used to select 50 officials from the Malawi Revenue Authority (MRA), the Ministry of Finance, Mota Engil Group representatives, as well as participants from civil society organizations (CSOs) such as the Malawi Economic Justice Network (MEJN), Tax Justice

Network Africa (TJNA) and African Tax Administration Forum (ATAF), as they possess critical insights into corporate taxation and policy enforcement. This approach guarantees a balanced and targeted selection of respondents, providing reliable and relevant data for the study.

DATA ANALYSIS AND INTERPRETATION



Scale of tax evasion by MNCs compared to other tax compliance issues in Malawi



Extent to which tax evasion reduces revenue

MAJOR FINDINGS

Findings revealed a widespread perception of underreporting of taxable income. About 36% of respondents stated that underreporting occurs often, while 25% believed it happens always. Together, 61% viewed tax underreporting as a persistent practice, suggesting that MNCs in Malawi systematically engage in tax avoidance. These perceptions align with Cobham and Janský (2018), who argue that MNCs frequently exploit weak tax enforcement in developing countries.

The finding also revealed the percentage of revenue that MNCs fail to declare, the largest proportion of respondents (43%) estimated this at 11–25% annually. Another 36% put it at 0–10%, while smaller groups suggested 26–50% or over 50%. These responses suggest a moderate yet significant level of revenue loss to the government each year.

The findings have also revealed that tax evasion by MNCs is a highly significant issue compared to other tax compliance problems. More than half (54%) rated it as "very significant," while 28% considered it "moderately significant." This indicates that tax evasion by corporations like Mota Engil is perceived as one of the most critical threats to Malawi's domestic revenue mobilization.

The economic impact of MNC tax evasion on government revenue, findings revealed strong consensus that corporate tax evasion severely reduces government revenue. Nearly 82% of respondents believed the impact was either "severe" or "significant." Only one respondent (2.3%) viewed it as minimal.

Estimates from secondary sources suggest that Malawi could lose up to USD 43 million annually due to tax evasion (ActionAid, 2013). With a tax-to-GDP ratio of about 13% (World Bank, 2022), this translates to 0.5–3% of GDP or MWK 100–200 billion. Such losses severely undermine Malawi's ability to fund public services, reduce aid dependency, and invest in development. The IMF (2014) and Cobham & Janský (2018) similarly argue that corporate tax evasion deprives developing countries of critical resources, worsening fiscal constraints.

SUGGESTIONS AND RECOMMENDATIONS

Given the prevalent perception that transfer pricing is the most common tax evasion method, future research should focus on a detailed analysis of how MNCs, including Mota-Engil, manipulate intra-firm transactions (e.g., overpricing imports or charging excessive management fees). This could involve case studies or forensic audits to quantify the scale and economic impact, providing concrete evidence to inform targeted policy reforms.

- Strengthening Transfer Pricing Regulations: Develop and enforce comprehensive transfer pricing rules aligned with international standards (OECD guidelines).
- Enhancing Audit and Investigation Capacity: Increase investment in the Malawi Revenue Authority (MRA) by training specialized audit teams in detecting complex tax avoidance schemes, including digital transactions and transfer mispricing.
- Strengthen Tax Audits and Enforcement Capacity**s**: Hire or consult with experts in MNC tax strategies and deploy technology (e.g., data analytics tools) to analyze financial records and cross-check MNC declarations against global benchmarks.
- Reform Tax Policies to Close Loopholes: Introduce a "unitary taxation" or "formulary apportionment" approach, allocating MNC profits based on real economic activity (sales, payroll, assets) in Malawi, rather than relying solely on self-reported subsidiary profits.
- Increase Penalties for Non-Compliance: Impose higher fines and penalties on MNCs found guilty of tax evasion or non-compliance with tax laws.
- Reviewing and Reforming Tax Incentives: Conduct an audit of tax incentives granted to MNCs and eliminate or reform those that are ineffective or abused

CONCLUSION

The study reveals a significant concern among respondents regarding the extent of tax evasion by multinational corporations (MNCs) in Malawi. A majority perceive underreporting of taxable income as a frequent or ongoing issue, with many believing that MNCs fail to declare a substantial portion of their revenue for tax purposes. The scale of tax evasion by MNCs is seen as a very significant problem compared to other tax compliance issues, indicating widespread concern over its negative impact on Malawi's economy.

Furthermore, the study highlighted the prevalent perception that multinational corporations (MNCs) in Malawi commonly use transfer pricing and tax incentives to evade taxes.Other tactics such as profit shifting, debt shifting, underreporting, and misinvoicing are perceived as less common but remain significant concerns. Additionally, it is suspected that Mota-Engil Malawi uses offshore subsidiaries or tax havens, particularly through transfer pricing, to minimize their tax liabilities. These findings align with global research on Base Erosion and Profit Shifting (BEPS), emphasizing the challenges Malawi faces in regulating MNC tax practices and the need for stronger tax enforcement and transparency.

The study concludes that tax evasion by multinational corporations like Mota-Engil significantly reduces Malawi's annual revenue, with 81.9% of respondents acknowledging the severe or significant impact of such practices. The Malawi Government faces substantial revenue losses due to methods such as transfer pricing, underreporting, and the abuse of tax incentives. Estimates suggest that Malawi could be losing between MWK 100 billion to MWK 200 billion annually, equating to 0.5% to 3% of its GDP.

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