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ECONOMIC ANALYSIS OF TAX EVASION: DETERIORATION AND SYSTEM OF CRIMINAL SANCTIONS IN BOSNIA AND HERZEGOVINA AND FEDERATION OF BOSNIA AND HERZEGOVINA

Abstract

This paper investigates the tax evasion through the lens of both classical economic theory and certain contemporary behavioral approaches, while maintaining focus on empirical data on relevant aspects of tax criminal policy, in both Bosnia and Herzegovina and Federation of Bosnia and Herzegovina (BiH). The analysis begins with the rational choice framework, where individuals, as Homo economicus, are modeled as utility-maximizing agents who weigh the expected benefits of evasion against the risks of detection and punishment.

In non-academic discourse in Bosnia and Herzegovina, there is a prevailing attitude regarding the "profitability" of committing tax offenses, which directly implies the inefficiency of existing criminal policy. This analysis will examine the classical Allingham and Sandmo deterrence model in the context of empirical data related to the suppression of tax evasion and criminal policy on tax-related criminal offences. Key findings show that suspended prison sentences and imprisonments of up to one year dominate in the structure of imposed criminal sanctions for tax-related criminal offences. Institute of substituting imprisonment with a monetary fine in criminal policy in BiH negatively affects general prevention in terms of tax-related criminal offences, since it allows for a replacement of imprisonment up to one year in prison for monetary fine. The statutory severity of the criminal sanction for tax evasion appears sufficient, but the severity of sanctions actually imposed by courts clearly points to a problematic psychological attitude toward tax evasion in Bosnia and Herzegovina: there seems to be a uniform perception of tax evasion as not being a particularly "serious" criminal offense, which indicates a high level of tax resistance among citizens.

Keywords: *Tax Evasion, Tax-related Crimes, Deterrence Model, Effectiveness of Criminal Policy, Rational Choice Theory*

I. Introduction

The fiscal system, regardless of the constitutional and political arrangement, represents one of the central pillars of state sustainability. Tax revenues dominate the structure of public revenues in modern states. The overall tax burden in each country is primarily viewed from the perspective of the adequacy of collected revenues to meet collective and general societal needs. The extensive definition of the state's role in directing socio-economic flows has been accompanied by an increase in the overall tax burden. It is precisely in the process of building the modern state that the tax burden begins to be researched and analyzed beyond the aspect of yield. This gives rise to the demand for determining the optimal level of the total tax burden in a way that will allow for an increase in social welfare, whether through the secondary distribution of income or by creating a stimulating framework for achieving economic growth.

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The law of diminishing returns is applicable to the issue of the tax burden: the tax burden has an upper limit and a decline in tax revenues occurs as a direct consequence when the prescribed tax burden exceeds that limit: either due to the legitimate abandonment of a profession or activity or due to illegal tax evasion.

One of the key problems is the size of the shadow economy (also referred to as the informal economy) and unfortunately, there is a lack of existing data estimating the total size of the shadow economy in Bosnia and Herzegovina. Various sources provide different statistical data, with most estimates indicating that the shadow economy in Bosnia and Herzegovina ranges between 31.22% and 47% of GDP (Asllani, Tzivanakis et Schneider, 2023). Informal economies in Central and Eastern European countries are estimated at around 26% of GDP, while former Soviet Union member states reportedly have informal economies as high as 45% of GDP (Gërxhani and Wintrobe, 2021).

Given the complexity of the factors that determine tax morale and tax evasion, the economic approach to the analysis of the legal system, more precisely of the tax system, enables a more thorough understanding of the effectiveness of specific legal provisions and a more adequate comprehension of taxpayer behavior. If viewed in the lenses of coherence, as a key legal principle, understanding the tax system requires directing the scope of the research towards provisions of the relevant criminal code, and actual criminal policy for tax offences in court's legal practice. The creation of models using economic analysis' tools contributes to a high-quality positive evaluation of the existing legislation and opens new avenues for empirical research aimed at confirming or refuting those models. This in turn results in normative recommendations for improving the efficiency of tax systems.

This paper represents an attempt to approach the issue of tax evasion by employing tools of economic analysis of law. The primary goal is to offer a complementary perspective to the classical legal understanding of the tax norm and criminal policy for tax offences, considering case law analysis and the theoretical model of deterrence.

II. Methodology

One of the key tenets of the economic analysis of law approach is the creation of the concept of the rational *Homo economicus*, which serves as the starting point for understanding rational decisions individuals make regarding their compliance with tax laws. In general, taxes represent an important determinant of behavior: the effects of taxation influence decisions related to work, savings, education and consumption, but can also potentially affect an individual's decisions to marry, divorce, the type and structure of investments in business entities and many other decisions (Stiglitz, 2004). In the literature, numerous factors influencing tax morale are frequently cited, which, as a subjective element of tax capacity, can often be linked to cultural or geographical affiliations. The level of education of taxpayers, the frequency of changes in tax regulations and the relationship of tax administration toward taxpayers, can also be viewed as determinants of tax morale (Sudžuka, 2020). Thus, the prevailing view in the literature is that the efficiency, rationality and transparency of the governing authorities, combined with the quality and catalog of citizens' social rights, significantly affect taxpayers' tax morale. Empirical evidence supporting this view is often drawn from examples of Scandinavian countries, particularly the Kingdom of Norway, which are characterized by high tax rates and simultaneously high tax morale among citizens.

Idea proposed by Kirchgässner in 1999 tries to explain the origins of the difference in tax moral in the *North* and in the *South*. Kirchgässner shapes initial standpoint by observing that in Northern Europe, the state and religious authority have historically been unified in one person, in contrast to Southern Europe, where the division between secular and religious authority, hence, the secular ruler (king) and the Church, was a defining feature of the social

and political order. Kirchgässner's idea emphasizes that the concept of sin has historically been an incentive for "aligning behavior" with tax norms (Gërxhani et Wintrobe, 2021). Returning to Homo economicus, his subjective stance regarding tax obligations is a clear example of a theoretical postulate of the economic analysis of law, where an individual follows their self-interest in an effort to maximize utility/profit; what is inherent in the logic of the taxpayer's relationship to all other costs associated with income/profit generation, is also inherent in the logic of the taxpayer's relationship to tax obligations. From the taxpayer's perspective, a tax obligation is an additional cost. In a certain context, the subjective stance of Homo economicus can be observed through an evaluation of the sociological elements of taxation.

The deterrence model proposed by Allingham and Sandmo is one of the most prominent models in academic debate and presents an initial starting point in the paper. This model conceptualizes tax evasion as a rational choice, grounded in considerations related to the probability of detection and punishment, the severity of the penalty and risk aversion (Allingham and Sandmo, 1972). A refinement of the model was introduced by Yitzhaki, who argued that the level of tax rates does not act as an incentive in the decision-making process regarding potential tax evasion: an observation commonly referred to in the literature as the Yitzhaki paradox. However, empirical studies have refuted Yitzhaki's model, confirming that reported income decreases as the tax rate increases (Folloni and Baldani-Miranda, 2024). The basis for Yitzhaki's assertion lies in the amount of tax evaded: as the total amount of evaded tax increases, the penalty for evasion also increases, thereby reducing the utility of the gains obtained through tax noncompliance when weighed against the threatened sanction. Yitzhaki's model is intuitive and although empirical data confirm a counterintuitive outcome in cases involving high tax rates and severe penalties for tax evasion, this model remains essential for understanding strategies in the design of punitive policy concerning tax-related criminal offenses.

The classic model establishes two key questions Homo economicus asks himself:

- What is the benefit from not adhering to tax laws and to what extent is exposure to the risk of being caught and sanctioned for illegal behavior?
- What criminal or administrative sanctions for illegal behavior are in force and how do they affect willingness to take on risk?

Introducing the variable of risk aversion, Homo economicus can also consider the question:

- What are the effects of illegal tax behavior on personal peace, social status and reputation in case of potential criminal procedure and conviction?

The fundamental idea is that in the process of generating income/profit, the decision to potentially evade tax obligations is a business decision, leaving room for the use of economic analysis of law as a primary tool for analyzing taxpayer behavior. The second question in the equation introduces risk aversion, without reallocation of the issue of decision-making beyond rationality. The taxpayer is still thinking about maximizing their utility and the loss of reputation represents a cost.

In case of Value-added Tax customer is not legally defined as taxpayer, however, still bears the cost of the indirect tax. The position of the individual that ultimately bears the tax burden is somewhat different and it is necessary to understand two distinct situations in the context of tax evasion related to VAT. In a situation where a subject, as a buyer/consumer of goods/services, is faced with the choice of paying for the goods/services with VAT included, receiving a valid fiscal receipt in accordance with fiscalization regulations (rules on cash registers, software's, issuance of receipts) or opting for an alternative choice where they pay for the goods/services without VAT included and do not receive a valid fiscal receipt, the

subject, following economic rationality and the tendency to maximize utility, might choose to purchase goods/services at a lower price, contributing to the growth of the shadow economy. This assumption is based on applying game theory concepts in economic analysis. This would hold true if the buyer does not need a fiscal receipt, so it is reasonable to conclude that this typically concerns individual consumers (citizens) as final buyers of goods or services. What is decisive in this scenario is the subject's clear awareness that they are participating in tax evasion based on their own intention to achieve the same benefit with a reduced cost. The subject is aware that the seller of the goods or provider of the services has withheld VAT and income/corporate tax payments due to the failure to record the transaction in the fiscal device.

Circumstances change significantly when the subject does not directly benefit from illegal arrangement/transaction. If the taxpayer sells goods/services to a subject, charging the price with VAT included, but at the same time does not issue a fiscal receipt (no record of the revenue), the subject will be deprived not only of the quality and scope of public services but also of the "savings" they would have had in the first situation. Tax morale and general citizen awareness and conscience play a significant role in the behavior of the subject who has been designated by the legislator to bear the burden of the consumption tax.

The critique of early models of economic analysis of law addresses the issue of neglecting non-economic determinants of taxpayer behavior. Tax policy measures aimed at raising awareness among final consumers about the need to take fiscal receipts address the second situation considered. Measures to combat the shadow economy by encouraging final consumers to take fiscal receipts when purchasing goods/services, which can be used to participate in so-called Receipt Lotteries organized by tax administrations, directly impact the suppression of the shadow economy in the second, and partly in the first, considered situation.

In the economic analysis of tax law, neglecting psychological elements can lead to the "empirical failure" of certain theoretical models. Thus, establishing additional costs for tax administration in terms of educating citizens can positively affect awareness about taking receipts. As already highlighted, in understanding the relationship between the taxpayer and tax obligations, the starting point is economic rationality, with key determinants in the decision to (non)comply with tax legislation being: the benefit derived from the illegal transaction, the probability of detecting tax evasion, the type and extent of criminal (administrative) sanctions and the taxpayer's willingness to take the risk of being caught and sanctioned. The hardest task in the economic analysis of tax evasion from the taxpayer's perspective is qualitatively and quantitatively determining the risk aversion. Numerous authors explain risk aversion by drawing parallels with gambling, where randomness plays a significant role in the decision-making process regarding potential tax evasion. It must be kept in mind that tax evasion also carries its own costs – double bookkeeping, the cost of taking actions that represent side effects of tax evasion, such as purchasing and transporting raw materials generating informal income/revenue.

Risk aversion and tax morale share a common denominator in the difficulty of quantifying them. The main difference between the two factors lies in the origin of their existence: risk aversion is a direct consequence of economic rationality and the desire to maximize profits. Homo economicus makes the decision on tax evasion and risk assessment rationally, so if they fear a criminal procedure and have an aversion to being suspected/accused, the benefit from tax evasion decreases. Tax morale does not solely originate in rationality and individualism: various cultural, religious, psychological and other exogenous ideological factors significantly influence the taxpayer in making the decision about potential tax evasion, where paying taxes is not valued based on the individualistic-rational reasoning of Homo economicus. Amartya Sen emphasizes that self-interest is not the only form of behavior that individuals adopt. One's own well-being is not the only value in human life and behavior that is not exclusively oriented toward self-interest is not necessarily irrational (Gërxhani et Wintrobe, 2021).

Transparency in the work of public authorities, rationality in public spending, trust in the government, the quality of public services and similar categories as factors of tax morale are endogenous in nature: *Homo economicus*, as a taxpayer, has trust in the state, so by paying taxes, he aims to increase his utility, which is reflected in the use of public services and vice versa. This approach to tax evasion offers a frequently contested theory of public choice. Despite the criticisms of such models, tax morale, as a social, economic and psychological determinant, must be, *a priori*, considered when discussing tax evasion.

Due to the complexity of the factors affecting the rational behavior of *Homo Economicus*, the model used in this paper focuses on the issue of the type and severity of criminal sanctions, concentrating specifically on imprisonment and the court's sentencing policy in practice. Based on the multitude of factors that affect the issue of the probability of detection, any potential research would, due to this multiplicity of factors, require a completely different, separate study as the object of the analysis significantly differs. The results of the present study, as well as any potential research in the context of the probability of detection, represent two dimensions of the classical Allingham and Sandmo model. At the level of sentencing policy, in relation to the Criminal Code of Bosnia and Herzegovina, the paper conducts an analysis of a range of tax criminal offences, while at the level of the Federation of Bosnia and Herzegovina, the focus is directed toward the criminal offence of tax evasion, as the most frequent and the most important tax crime.

III. Tax evasion and legal framework in Bosnia and Herzegovina

Modern state's criminal codes contain some form of tax-related criminal offenses, typically systematized either in a separate chapter of the criminal code (Tax crimes) or general chapter on economic crimes. In BiH, both models are present, as there are four existing criminal codes enforced: The Criminal Code of Bosnia and Herzegovina includes, in its special section, Chapter XVIII "Criminal Offenses Against the Economy and Market Integrity and Offenses in the Area of Customs." The Criminal Code of the Federation of Bosnia and Herzegovina contains Chapter XXIII "Criminal Offenses in the Area of Taxation" and the same structure is present in the Criminal Code of the Brčko District of Bosnia and Herzegovina. The Criminal Code of the Republic of Srpska contains Chapter XXI "Criminal Offenses Against the Economy and Financial Transactions." At the same time, there are differences in the content of the subject chapters, since classification of criminal offenses is not entirely identical, however, tax evasion is classified and regulated identically. This is due to the fiscal decentralization in BiH. Indirect taxes (VAT, excise and customs) are collected at the State level (Bosnia and Herzegovina), while direct taxes are collected at the entity (FBiH, RS) and Brčko District level. Certain criminal offenses, tied to specific indirect taxes, are only regulated at the State level, as indirect taxes fall exclusively under the competence of the State of BiH.

The criminalization of tax-related offenses stems from the necessity to establish protection of the state's fiscal sovereignty. Jovašević points out that legal literature broadly supports the view that tax evasion, *lato sensu*, is a specific form of fraud. In any case, the object of protection for these criminal offenses is the state's fiscal system and the collection of public revenues (Jovašević, 2018). In the criminal legislation of BiH, *dolus directus* is the constituent element of tax-related criminal offenses such as tax evasion or tax fraud. Tax-related criminal offenses are of a blanket nature (blanket provisions), meaning that their establishment and fulfilment require a violation of certain tax law provisions. Since such violations may also constitute misdemeanors, which fall under misdemeanor law, a clear objective criterion is needed in practice to distinguish between a tax-related criminal offense and a tax-related misdemeanor. Misdemeanor procedure in Bosnia and Herzegovina's legal system consists of legal proceedings in case of unlawful acts or certain violations of law, where such violations are less

intensive that criminal offenses, thus, penalty for violation is less severe than in case of criminal offenses.

Based on the need to distinguish between a misdemeanor and the constitution of a criminal offense, various criteria are established in comparative legislation. In criminal law theory, this is referred to as the objective condition of incrimination, meaning that there is a substantive legal requirement (objective criterion) that tax payment was unlawfully evaded in a certain amount (threshold). If that amount as threshold is exceeded, the elements of a criminal offense are fulfilled, otherwise, it is a matter of a tax-related misdemeanor. Thus, in the criminal legislation of BiH and FBiH, the objective (substantive) condition for incrimination is defined as the evasion of tax payment in an amount exceeding 10,000 BAM (5.113 EUR). For example, the Criminal Code of the Republic of Croatia prescribes a significantly lower amount of EUR 2.654,46. This distinction has significant practical implications: potential errors during tax inspection in case of violation of tax law provisions where subject tax was evaded in the amount exceeding 10,000 BAM could result in misdemeanor. In such a scenario, misdemeanor combined with the principle of *ne bis in idem*, prevents the imposition of a criminal sanction. Lastly, the factual nature of tax evasion as a criminal offense is of relevance to this analysis. Namely, due to the factual actions undertaken with the aim of evading tax payment, in practice tax evasion is often followed by the fulfilment of the elements of an additional criminal offense, typically in the form of falsification of business/commercial records, forgery of documents, etc. (Cipek, 2018).

1. Tax-related Offences in Bosnia and Herzegovina and Federation of Bosnia and Herzegovina

Regarding the Criminal Code of BiH, tax tax-related criminal offenses are systematized under Chapter XVIII “Criminal Offenses Against the Economy and Market Integrity and Offenses in the Area of Customs”. Tax-related criminal offences, at the State level, from Chapter XVIII, are presented in Table 1. with prescribed criminal sanctions. In the Criminal Code of FBiH, tax-related criminal offenses are systematized under Chapter XXIII. Article 273 of the Criminal Code of FBiH prescribes the offense of tax evasion, Article 274 the offense of false tax documentation, Article 275 the offense of improper allocation of funds by legal persons, Article 276 the offense of submitting false tax returns, Article 277 the offense of obstructing a tax official in the performance of official duties and Article 278 the offense of assaulting a tax official while performing official duties. Legal framework and prescribed criminal sanctions are presented in Table 2. Even though the systematization differs, it can be concluded that the harmonization of criminal sanctions is evident, where criminal offenses are only partially harmonized due to the division of the fiscal competences between the State (indirect taxation) and the entities (direct taxation).

Table 1. Tax-related crimes in Criminal code of BiH with prescribed sanctions

| Article and Tax crime | Criminal sanction | Criminal sanction for the qualified form of the criminal offence |
|---------------------------------------|--|--|
| 210 Tax Fraud and Evasion | Imprisonment: 6 months – 5 years | Imprisonment: 1-10 years, at least 3 years |
| 210a Illicit trade in excise goods | Imprisonment: 6 months to 5 years | - |
| 210b Unlawful storage of goods | Monetary fine or Imprisonment up to 3 years | Imprisonment: 1 to 10 years |

| | | |
|--|--|---|
| 214 Smuggling | Monetary fine or Imprisonment up to 3 years | Imprisonment: 6 months to 5 years, 1 to 10 years |
| 215 Organizing a group or association for smuggling or distribution of untaxed goods | Imprisonment: at least 3 years for Organizer and 1 year for Group Member | - |
| 216 Customs fraud | Monetary fine or Imprisonment up to 3 years | Imprisonment: 1 to 10 years, at least 3 years |

Table 2. Selected Tax-related Crimes in Criminal code of FBiH with Prescribed Sanctions

| Article and Tax crime | Criminal sanction | Criminal sanction for the qualified form of the criminal offence |
|---|--|--|
| 273 Tax evasion | Imprisonment: 6 months to 5 years | Imprisonment: 1 to 10 years. Imprisonment: at least 3 years |
| 274 False tax documentation | Monetary fine or Imprisonment for up to 1 year | Monetary fine or Imprisonment up to 3 years |
| 275 Improper allocation of funds by legal persons | Monetary fine or Imprisonment up to 3 years | - |
| 276 Submitting false tax returns | Monetary fine or Imprisonment up to 3 years | - |

2. Replacement of Prison Sentence with a Fine and Purpose of Punishment

Replacement of prison sentence with a monetary fine has been introduced in the Criminal Code of FBiH in 2010 (Official Gazette of FBiH, no. 42/10). In accordance with the article 43A, a sentence of imprisonment of up to one year, may, at the request of the convicted person, be replaced with a fine by equating each day of the sentence of imprisonment with one daily fine or with 100 BAM, which should be paid in a lump sum within a period of up to 30 days, under the threat of execution of the sentence of imprisonment. In 2025 (Official Gazette of FBiH, no. 58/25), amount of the fine increased from 100 BAM (51.13 EUR) to 150 BAM (76.70 EU). Therefore, the monetary amount that replaces a prison sentence of up to one year was increased from 36.500 BAM (18.662 EUR) to 54.750 BAM (27.902 EUR) on the annual basis (1 year imprisonment). The same legal solution is also present in the Article 42A of the Criminal Code of Bosnia and Herzegovina, however, the amount of the daily fine never increased, meaning original provisions are still applicable (100 BAM).

In the other BiH's entity, the Republic of Srpska, the legal situation drastically shifted in 2025 when the Constitutional Court of Republic of Srpska in Decision no. U-77/24 of 24 September 2025, published in the "Official Gazette of RS", no. 85/2025, declared Article 46a unconstitutional, as the relevant provision on the replacement of the prison sentence with a monetary fine, placed convicted persons of better financial standing in a more favorable position, enabling them to avoid serving a prison sentence. On the contrary, those of weaker economic status were effectively deprived of the same possibility. Replacement institute, as viewed by the Constitutional Court of RS, does not leave room for the court to decide on the basis of the circumstances of the specific case, whether the replacement is justified *in concreto*.

Apart from the discrimination aspect, the Decision emphasized the correlation between the purpose of the punishment and the institute of replacement of the prison sentence with a fine. Two important principles are accordingly affected: the principle of fairness and the principle of individual approach to sentencing. To this date, same legal logic was not applied at the State level and in the FBiH. The relevant provisions remained enforced and intact in the Criminal Code of BiH and FBiH. A potentially identical position of the Constitutional Court of Bosnia and Herzegovina, or of the Constitutional Court of the Federation of Bosnia and Herzegovina, would significantly affect the findings of the present study which is addressed in the discussion section of the paper.

Purpose of punishment is defined in Article 39 of the Criminal Code of BiH. In accordance with the Article 39, purpose of punishment is to “express social condemnation of the committed criminal offense, general prevention and special prevention, as well as to “influence the awareness of citizens about the dangerousness of criminal offences and the fairness of punishing the perpetrator” (Criminal Code of BiH 2003). Same concept regarding the purpose of punishment, and same legal solution is present in Article 42 of the Criminal Code of FBiH.

IV. Results and discussion

Data on criminal sanctions was provided by the Court of Bosnia and Herzegovina and the High Judicial and Prosecutorial Council (VSTV) and processed for the analysis. Data is shown in Table 3 and 4 below.

Table 3. Imprisonment and Avoided imprisonment for Tax crimes: Court of BiH 2020-2024

| Article and Tax Offence | Avoided imprisonment (convicted individuals) | Imprisonment (convicted individuals) | Imprisonment in case of multiple offences |
|--|--|--------------------------------------|---|
| 210 Tax Fraud and Evasion | 63 | 9 | 2 |
| 210a Illicit trade in excise goods | 207 | 3 | 2 |
| 210b Unlawful storage of goods | 19 | 0 | 0 |
| 214 Smuggling | 51 | 6 | 3 |
| 215 Organizing a group or association for smuggling or distribution of untaxed goods | 2 | 1 | 1 |
| 216 Customs fraud | 1 | 1 | 1 |
| Total number of convicted individuals | 343 | 20 | 9 |
| Total number of analyzed final legally binding Court's decisions | 327 | | |
| Percentage of convicted individuals | 94.49% | 5.51% | |

Source: Court of BiH 2025, Own analysis

Table 3 presents data on criminal sanctions imposed by the Court of Bosnia and Herzegovina for tax-related criminal offences in the period 2021–2024. These are final legally binding court decisions. The imposed criminal sanctions were analyzed for offenders who were

found guilty of tax-related criminal offences in a total of 327 different cases before the Court that were analyzed. In certain cases, multiple persons were convicted in a single conviction, hence, the number of analyzed court decisions is smaller compared to total number of individuals convicted.

The focus of the analysis of the cases in question was directed toward the issue of the possibility of avoiding the serving of a prison sentence. If, on any legal basis, an offender convicted of a tax-related criminal offence was able to avoid serving a prison sentence, the case was recorded as an avoided prison sentence (Convicted individuals that avoided or could have avoided imprisonment under existing legal provisions of the Criminal Code). The legal bases in the given cases are a suspended prison sentence, a prison sentence of up to one year, which accordingly is subject to the institute of replacement of a prison sentence with a fine, or an imposed monetary sanction where it is prescribed as an alternative criminal sanction to imprisonment.

63 offenders, found guilty of the criminal offence of Tax Fraud and Evasion (Article 210), avoided, or were able to avoid, serving a prison sentence, while only 9 of them had to serve the prison sentence. Data for other tax-related criminal offences is presented in Table 3. According to the stated data, as many as 94.49% of convicted persons, found guilty of tax crime, avoided, or had the statutory possibility of avoiding, the serving of a prison sentence. Only 5.51% of convicted persons neither avoided nor had the possibility of avoiding the serving of a prison sentence. The far-right column represents a total number of imprisonments in cases when convicted persons were found guilty of multiple offences, and this number is included in total recorded imprisonments shown in the middle column.

Table 4. Imprisonment and Avoided imprisonment for Tax Evasion (Article 273 of Criminal Code of FBiH): Courts of FBiH 2020-2024

| Article 273 – Tax Evasion | Avoided imprisonment | Imprisonment |
|---|-----------------------------|---------------------|
| Convicted individuals and Imprisonment (Article 273 all forms of a criminal offence) | 30 | 18 |
| Percentage out of total number of convicted individuals | 62.5% | 37.5% |
| Convicted individuals and Imprisonment: Aggravated form of a criminal offence – Article 273 (2) | 3 | 1 |
| Convicted individuals and Imprisonment: Aggravated form of a criminal offence – Article 273 (3) | 0 | 12 |
| Number of convicted individuals that have avoided imprisonment via replacement institute | 1 | 0 |
| Number of Confiscation of unlawfully obtained property | 4 | |
| Prohibition on the performance of a profession, activity or function | 1 | |
| Total number of analyzed Court’s decisions | 43 | |

Source: High Judicial and Prosecutorial Council of BiH (VSTV) 2025, Own analysis

Table 4 presents data on imposed criminal sanctions and measures before the courts of the Federation of Bosnia and Herzegovina (municipal courts, cantonal courts, and the Supreme Court of the Federation of Bosnia and Herzegovina) in the period 2020–2024 for the criminal

offence of tax evasion under Article 273 of the Criminal Code of the Federation of Bosnia and Herzegovina. A total of 43 cases were analyzed. According to the data analyzed, 62.5% of perpetrators of the criminal offence of tax evasion *de facto* avoided serving a prison sentence, on the basis of the institute of suspended sentence as a warning measure (29 convicted persons), or on the basis of substitution of imprisonment with a monetary fine (1 convicted person). Of the total number of convicted individuals, only 37.5% failed to avoid a imprisonment. In this respect, 13 out of a total of 18 (72.22%) were convicted of the aggravated form of the criminal offence of tax evasion (Article 273(2) and Article 273(3)). Confiscation of unlawfully acquired pecuniary gain was applied in 4 cases.

By adhering to the legally prescribed criminal sanctions for criminal offences in the field of taxation, it can be stated that the type of criminal sanction, as well as the sentencing range, is set adequately, which may potentially influence deterrence in accordance with the Allingham–Sandmo model. However, judicial practice with regard to the severity and type of sanctions indicates significant problems in deterring potential offenders.

In judicial practice in both BiH and FBiH, suspended prison sentences and imprisonment of up to one year dominate. In the latter case, combined with the institute of replacement of imprisonment with a monetary fine, general prevention is negatively affected. Also, confiscation of unlawfully obtained property occurs rarely in criminal proceedings (only four identified confiscations in relation to tax crime in FBiH in the observed time frame 2020-2024). From the perspective of a rational decision made by *Homo economicus*, the math is clear: *If I am sentenced to prison for up to one year, the monetary gain will be confiscated, and I will be able to avoid imprisonment by paying 36,500 BAM (1 day = 100 BAM).*¹ From economic analysis of law standpoint, even further conclusion can be made regarding the type of evaded tax. As the fine in case of replacement of imprisonment is lower at the State level (Criminal Code of BiH) compared to the FBiH level (Criminal Code of FBiH), the difference incentivizes individuals to evade indirect taxes, such as customs and VAT, as those taxes are collected at the State level.

The statutory severity of the criminal sanction for tax evasion appears sufficient, but the severity of sanctions actually imposed in judicial practice clearly points to a problematic psychological attitude toward tax evasion in Bosnia and Herzegovina: there seems to be a uniform perception of tax evasion as not being a particularly "serious" criminal offense, which indicates a high level of tax resistance among citizens. Despite the existence of important political and legal assumptions that the state could act upon to reduce resistance, there is also the impression that the violation of the fiscal system as the object of protection is not seen as a significant violation in the eyes of the courts. It is impossible to neglect the cause of this attitude. The actual question that arises is connected to the appointed judges: *Do appointed judges possess adequate knowledge on the fiscal system, its meaning and importance?* Furthermore, additional question is: *Do judges understand who, how and when, creates new economic value and how revenues, eventually used for administration funding, are collected in the first place?* It would be useful to publish annual reports on indicators of tax evasion and relate quantitative estimates to the number of schools, hospitals, parks, or kilometers of highway that could be built with that money. This could potentially affect awareness.

One of the solutions present in some legal systems concerns the introduction of a progressive monetary fine. Such a fine, in correlation with Yitzhaki's modification of the classical model, can serve more effectively in prevention. The key dilemma from the standpoint of tax evasion is the efficiency of deterrence and strengthening inspection/investigative oversight in practice. Despite the fact that imposing higher/harsher penalties for tax crimes does not place additional costs on the budget, while strengthening law enforcement in practice

¹ In FBiH, daily amount is 150 BAM and 54.750 BAM on an annual basis.

does imply additional budgetary expenditures, without an adequate oversight and control mechanism that increases the certainty of detecting tax evasion, the prescribed penalty alone cannot adequately "frighten" a potential perpetrator - even if the penalty were life imprisonment. Multiplying by zero results in zero. If *Homo economicus* is reasonably confident that there are many worse offenders ahead of him in line for prosecution, multiplying any prescribed penalty by a 0% probability of detection yields a 0% effectiveness of the deterrence model, regardless of the severity of the penalty. Thus, it is necessary to conduct additional research on the enforcement of tax law, as detection of tax evasion is a prerequisite for the criminal proceeding at first place. Nevertheless, analyzed court cases, at the level of BiH and FBiH, clearly indicate low possibility of deterioration.

Alternatively, *Homo economicus* is reasonably confident that he will be sentenced to prison for up to one year and will ensure his freedom by replacing the imprisonment sentence up to one year with a monetary fine. Regarding the criminal policy for tax crime in case of Court of BiH, as suspended prison sentences absolutely dominate in analyzed cases, deterrence effect is even significantly lower. According to the data stated at the level of BiH, 94.49% of convicted persons for various forms of tax crime avoided or had the statutory possibility of avoiding a prison sentence. Empirical evidence is *relentless* in this case: if 9 out of 10 convicted individuals can avoid imprisonment, risk aversion does not provide for deterioration that could effectively prevent *ordinary individuals*, with *ordinary risk aversion*, from committing tax offences. Only the interplay of criminal policy of the courts, and the enforcement policy of tax administration, provides for a clear picture on risk aversion. Although separate empirical study in connection with enforcement of tax policy is needed, results obtained in this research prove lenient penal policy heavily incentives potential tax offenders, irrelevant of the statistic chance for detection of tax offences in practice. Even in case of high detection possibility, once that individual is charged for tax offence, the result of criminal proceeding when individual is found guilty, cannot be compensated. If it was the other way around, the logic differs. For example, if detection possibility is low, and criminal policy in effect is stringent, *Homo economicus* would calculate with the risk in a different way. Even though he will not be detected easily, if his felony is eventually detected, he is likely going to serve prison sentence. This is why stricter criminal policy is *conditio sine qua non* when considering risk aversion of the potential tax offender.

Despite certain differences in the legislative definition of the purpose of punishment in the Criminal Code of the Republic of Srpska, compared to the provisions of the Criminal Codes of Bosnia and Herzegovina and the Federation of Bosnia and Herzegovina, considering the legal scope of the purpose of punishment in criminal codes of BiH and FBiH, it is possible to take the position that the reasoning of the Constitutional Court of the RS is much stronger in the context of the criminal codes of BiH and FBiH. If the same legal position is undertaken by relevant constitutional courts in foreseeable future, purpose of the punishment will be enhanced considering tax fraud and other tax-related offences.

It is appropriate to point out that increasing the frequency of the application of the institute of confiscation of unlawfully acquired pecuniary gain based on the commission of a criminal offence in the future period could make a positive contribution at the level of deterrence, although the application of this institute brings additional complexity of, already complex, financial investigations. The application of this institute has great potential within deterrence policy, given that, at the core of the motive for committing criminal offences in the field of taxation, there is always pecuniary gain as an imperative. By imposing annulment of this pecuniary gain in criminal proceedings, through confiscation of unlawfully acquired pecuniary gain, risk aversion, from the classic Allingham and Sandmo model, would heavily increase. Separate study could, using economic analysis of law, focus on the *optimal level of confiscation*. As confiscation means that financial investigation becomes more complicated, additional funds

are needed to conduct the confiscation. Increasing funding for financial investigation would result in more confiscation of unlawfully acquired pecuniary gain in practice, however, at some point, logic of marginal costs determines the optimal level of confiscation.

Considering the results obtained from the analysis of the cases from FBiH's court, it is hard to *miss* the uneven geographical distribution of the cases. There are no cases of convictions for tax fraud in Bosnian-Podrinje Canton Goražde, Posavina Canton, West Herzegovina Canton and Canton 10. This is a meaningful indicator regarding uneven distribution of tax inspection and enforcement of tax policy in FBiH. Thus, any potential research that focuses on detection, including both tax inspection and criminal investigation, would need to address this issue.

V. Conclusion

More comprehensive and narrow analysis of criminal policy for tax related offenses would result in clearer recommendations for addressing the issue of tax evasion and the grey economy. However, considering the empirical findings in the subject research *en gros*, criminal policy in the courts' practice in BiH and FBiH toward tax offenders tends to be lenient, if not completely inadequate. Most convicted individuals manage to avoid imprisonment, mostly due to excessive usage of suspended prison sentences. Furthermore, the institute of replacement of imprisonment with fine, in case of tax offences, seems illogical as pecuniary gain is the criminal motive in case of tax evasion. Low to non-existent confiscation of unlawfully acquired pecuniary gain in criminal proceedings in case of tax offences just adds *an additional layer of* illogicality. If institute of confiscation was more frequent in criminal proceedings, the illogical aspect of the institute of replacement of imprisonment with fine would be minimized.

There are three potential solutions to the identified problem. One is a comprehensive reassessment of the existing penal policy in courts' practice, in terms of reconsidering the type and severity of criminal sanctions and warning measures. It appears that the use of the suspended sentence, as a warning measure, is excessively extensive in practice. The second potential solution would be the introduction of a progressive monetary sanction as a counterbalance to the pecuniary gain that is always present in tax-related criminal offences. Third, limiting or abolishing the institute of substitution of imprisonment with a monetary fine would, in practice, create preconditions for more effective general and special prevention. Purpose of punishment, as defined in Article 39 of the Criminal Code of BiH, needs to establish the concept of fairness of punishing the perpetrator. However, both institute of replacement, as well as extensive usage of suspended prison sentences, negate this purpose from the author's view. The range of sanctions sentenced by courts clearly points to a misunderstanding of the aim and purpose of punishment for tax crimes and omission of its fiscal dimension.

One psychological factor also needs to be emphasized. The question arises: *Does less intensive penalization of individuals committing tax evasion offenses pose to be a negative incentive on state bodies that conduct criminal and/or financial investigation?* As was mentioned in the introduction of Allingham and Sandmo model, the possibility of detection of tax evasion is an integral part of the model, however, the question implies possibility that lenient penalization dissolves coherence in the internal relations of different state authorities, where the result is low motivation of the investigation authorities. In the context of FBiH, this question needs to be understood *in light of* legal barriers that already diminish efficiency of tax authorities in conducting investigation.

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Tables

Table 1. Tax-related Crimes in Criminal code of BiH with Prescribed Sanctions

Table 2. Selected Tax-related Crimes in Criminal code of FBiH with Prescribed Sanctions Table 3. Imprisonment and Avoided imprisonment for Tax crimes: Court of BiH 2020-2024

Table 4. Imprisonment and Avoided imprisonment for Tax Evasion (Article 273 of Criminal Code of FBiH): Courts of FBiH 2020-2024