1. INTRODUCTION

Taxpayer behaviour, particularly in respect of compliance, has been a subject of a great deal of research emanating from a wide range of disciplines for more than thirty years now. However, in spite of the breadth and mass of literature that has emerged, the fundamental problem, of being able to understand why taxpayers behave in the way that they do, remains largely unsolved. Instead, what has come to light is a growing acceptance of the view that people are complex creatures who behave in ways that are difficult to understand and predict.

At the same time, the need for tax administrations to understand compliance behaviour remains as important as ever, with noncompliance being a global phenomenon that can threaten the integrity of any and every tax system. Administrations must develop and implement strategies to improve taxpayer compliance. However, the effectiveness of such strategies is hampered by the lack of progress in understanding the behaviour to be addressed. Clearly, this is an area of enormous challenge for both researchers and administrations.

The purpose of this paper is to present and analyse the findings of a behavioural study of Australian personal income taxpayers in order to identify positive strategies for improving compliance. The study is narrow in its focus in that it addresses only one type of taxpayer and its applicability to other types of taxpayers, even in the Australian context, is unknown. However, given that personal taxpayers in Australia comprise approximately 85 per cent of total income taxpayers and are the source of over 70 per cent of net tax payable, they are a significant body. It is also believed that the findings of this study have relevance to other regimes that will no doubt recognise the similarities that may exist and evaluate the suggested strategies accordingly.

The body of the paper follows and is presented in three parts. The first part provides the rationale for the study. It includes an overview of the compliance literature relevant to the study, the logic and scope of which is outlined. The second part justifies the use of the multi-paradigm research method employed and presents those findings considered to be most significant and reliable. The third and final part considers the implications of these findings for Australian tax administration: including the Australian Taxation Office (ATO), Treasury, Parliamentary Counsel and Government, and how these findings could inform the development and implementation of strategies to improve taxpayer compliance.

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1 See Brooks, N., 1998, “The Challenge of Tax Compliance” in Evans, C. and A. Greenbaum (Eds.), Tax Administration: Facing the Challenges of the Future, Prospect, Sydney at 7-33. Brooks (p.22) stated that what we have ended up learning from compliance research is “how much we do not know”.


3 Personal taxpayers include all individuals in receipt of income other than those engaged in carrying on a business.

2 RATIONALE

As previously noted, the body of literature on taxpayer behaviour is extensive and it is not the intention here to review it fully as this has been done previously. Instead, the approach taken is to reflect on three major themes in the literature that are considered directly relevant or formative to this study.

Firstly, compliance and noncompliance are now recognised as being outcomes of which many variations or dimensions exist. Much of the earlier literature focused on noncompliance as being of one dimension only, namely intentional tax evasion, and studied the means by which to address it. However, over time, there has been an emerging recognition that not all noncompliance is necessarily intentional. Given the many variations of both compliance and noncompliance, it follows that in developing appropriate strategies to modify taxpayer behaviour, the tax administration must clearly identify the behavioural outcome that it seeks to address.

Secondly, the continued pursuit of a single-overarching theory of compliance behaviour appears more than ever to be an idealistic exercise. Realistically, if such a theory could ever be developed and adequately proven, it would require a complete understanding of the relationships, over time, between many independent variables (which may or may not be known) and an array of dependent variables, or outcomes. It would also need to take into account the influence of mediating variables, such as demographics, on these relationships.

Further, such a theory would need to incorporate the different types of taxpayers, and the roles played by the various parties including taxpayer, tax agent and tax administration. However, even if such a theory could exist, it would serve little practical purpose as it would require the tax administration to be able to identify the independent variables and, more importantly, to be able to control them in order to modify the outcomes.

Thirdly, there is little consensus as to appropriate research methods in the study of taxpayer behaviour, with many studies having acknowledged weaknesses including definitional issues, access to appropriate data sources and validity. However, there does appear to be greater confidence in studies based on limited variables related to a conceptual base, randomised experiments and observations of real-life behaviour, rather than those based on self-reports, simulations or hypothetical situations.

Against this background, it appeared that the study of a narrowly defined behavioural outcome using a stronger research method, held considerable promise in terms of advancing the understanding of

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8 For example, see Long and Swingen at note 2, Kidder and McEwen at note 6.

9 See Long and Swingen at note 2.

Taxpayer behaviour. The behavioural outcome chosen for this study was unintentional noncompliance. That is, where taxpayers formed the intention to be compliant, but the eventual outcome was otherwise. This outcome was selected for a number of reasons, one being that it did not necessitate the study of how intent was formed and influenced behaviour, an area of literature that is both extensive and inconclusive. More importantly, this outcome was chosen because it was felt that ‘complexity’, whatever its manifestations, was both the most likely cause of unintentional noncompliance, and the one variable that could be readily controlled, or at least influenced, by the tax administration. Therefore, addressing the causes of ‘complexity’ had potential as a strategy for achieving timely and efficient improvements in compliance outcomes.

Taxpayers whose compliance behaviour was considered the most likely to be influenced by complexity were those who lodged their own income tax returns, rather than use the services of a tax agent. In Australia, personal taxpayers are the only category of taxpayer where self-preparation of income tax returns still occurs to any extent. Even so, for personal taxpayers the use of a tax agent has remained relatively constant at around 75 per cent for over a decade, making them probably the most agent-dependent group in the developed world. This high use of a tax agent by personal taxpayers in Australia may well be caused by complexity. Apart from seeking to address unintentional noncompliance, studying the influence of complexity could facilitate cost savings in compliance, administration and enforcement.

The study was therefore limited to personal taxpayers in Australia. Its purpose was to understand how complexity influenced their compliance behaviour, with unintentional noncompliance being of specific interest.

3. RESEARCH METHOD

A multi-method research design was implemented, drawing on the strengths of both the quantitative and qualitative paradigms. The quantitative component utilised a randomised mail survey of personal taxpayers, made possible with the co-operation of the ATO and the Taxpayers' Research Foundation (TRF). The TRF fulfilled the role of intermediary to ensure that taxpayers' privacy was maintained, and also provided assistance by way of a research grant. It was envisaged that this component of the study would facilitate the making of statistical generalisations.

In contrast, the qualitative component would facilitate the making of analytical generalisations. This component was based on repetitions of a case study protocol conducted in a real-life context, that included compliance judgements to be made by the researcher (an experienced certified practising accountant and registered tax agent) based on the examination of tax returns and supporting evidence prior to lodgement. This was an important aspect of the study as taxpayers could not be expected to

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13 For a more comprehensive justification of the research method see McKerchar at note 2.
identify their behaviour as being unintentionally noncompliant, nor was the tax administration considered well placed to make this judgement based solely on the tax return.14

Together, the quantitative and qualitative components were expected to complement and inform each other, thereby providing a deeper understanding of both the process and outcomes of return completion. Further, should there be a convergence of results from the two components, greater confidence in the overall findings would be possible.15

In applying the research method, the approach taken was to deconstruct the research problem into a range of descriptive, secondary and primary questions as presented at Figure 1. Descriptive questions principally addressed the definitions used in the study, including the dimensions of complexity, and presented descriptive findings. Secondary questions addressed the influence of nine mediating variables, drawn largely from the literature, on the five primary areas under consideration.16 The mediating variables used in this study were gender; age group; level of income; type of income; highest level of education completed; whether or not the taxpayer had dependants; residential location (being either metropolitan or non-metropolitan); language normally spoken at home (being English or non-English); and the type of completer (whether the return had been completed by the taxpayer, a tax agent, or another third party).

The primary variables under consideration were complexity and those areas that complexity was considered most likely to have an influence, namely compliance outcome (or confidence in accuracy of tax return where the outcome was unknown), commitment to compliance, perception of fairness, and compliance costs (including non-monetary costs such as time, stress and anxiety).17 In the context of this study, the meaning of compliance costs was in accord with that developed by Adam Smith, including the cost of vexation which, while not strictly an expense, was included in what a person would willingly pay to be redeemed from the "..odious examination of the tax gatherers".18 The primary questions studied the relationships between these five areas in terms of cause and effect. All research questions were addressed from both paradigms wherever feasible.

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14 This view was based on a study conducted in co-operation with the Office of the Tax Inspectorate, Rotterdam as reported in Hessing, D., Elffers, H. and R. Weigel, 1988, “Exploring the Limits of Self-Reports and Reasoned Action: An Investigation of the Psychology of Tax Evasion Behaviour”, Journal of Personality and Social Psychology, 54 at 405-413.

15 Creswell, J., 1994, Research Design: Qualitative & Quantitative Approaches, Sage, Thousand Oaks CA. Jackson and Milliron (at note 10) noted that multi-method studies held promise of improving future compliance research, though there is little, if any, evidence in the tax compliance literature of such studies.


17 The relationship between complexity as increasing compliance costs and discouraging compliance had previously been theorised by Slemrod, J., 1989, “Complexity, Compliance Costs and Tax Evasion” at 156-181 in Roth and Scholz at note 6.

Figure 1: Diagrammatic representation of the research problem

What is the impact of complexity upon (unintentional non-)compliance?

<table>
<thead>
<tr>
<th>PROBLEM</th>
<th>DESCRIPTION</th>
<th>DIRECT RELATIONSHIP</th>
<th>MEDIATING VARIABLES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cause</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Complexity</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Effects</td>
<td></td>
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<td></td>
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<tr>
<td>Compliance</td>
<td></td>
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<td>outcome and confidence</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>Commitment to compliance</td>
<td>Self-ranking</td>
<td></td>
<td></td>
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<tr>
<td>Perception of fairness</td>
<td>Self-ranking</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Compliance cost</td>
<td>Self-measurement</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

The four direct relationships will then need to be studied for the impact of mediating variables.

The mediating variables are:
- Gender
- Age
- Level of income
- Type of income
- Level of education
- Dependent status
- Residential location
- First language
- Type of completer

M McKerchar
3.1 Quantitative component.

The ATO extracted two random samples, 600 in each, from its database of personal taxpayers who had either lodged or were expected to lodge an income tax return for the year ended 30 June 2000. The samples were divided according to those who had last lodged through a tax agent and those who had not. The response rates to the survey were higher than expected, 50.6 per cent for those who lodged via an agent and 57.4 per cent for those who lodged their own return. Of those who lodged their own return (n = 340), 24 per cent indicated that another person (family member, friend or colleague) had completed the return on their behalf. The respondents were compared to the sample frame on the basis of age group, gender and State of residence and were found to be a reasonable representation of the broader population of personal taxpayers in these respects.

Three key areas of the analysis of the survey results are presented herein: the findings in respect of the causes and extent of complexity, the impact of the mediating variables, and the relationships between the primary areas under consideration.

3.1.1 Complexity.

Complexity was said to have arisen wherever a personal taxpayer reported any difficulty in completing his or her own tax return for the year. In Australia, the method by which this is normally done is by the use of an instructional booklet provided by the ATO, known as TaxPack (128 pages in length in 2000). In addition, where taxpayers have income from other sources such as rental income or a capital gain, a supplementary booklet (68 pages in length in 2000) is also required. Separate return forms are required for both TaxPack and its supplement. Almost 50 per cent of the relevant respondents reported that they had not experienced any problems in completing their tax return.

For those respondents who had completed their own return and had encountered problems, questions were asked to determine the most common cause(s) of complexity and of the most difficult problems encountered. These questions were based on the work of Long and Swingen with tax agents, where the following six potential causes of complexity were identified:

- ambiguity (or uncertainties in the law lead to more than one defensible position);
- computations (many or difficult computations to be made);
- change (there have been frequent or recent changes to the law);
- detail (there are numerous rules and exceptions to the rules);
- record keeping (detailed special records must be kept); and

19 The total sample frame of personal income taxpayers in Australia as at the extraction date of 11 May 2001 was 9.1M, of which 6.8M lodged through a tax agent.
20 By way of comparison, two recent random mail surveys conducted in Australia (Evans, C. Ritchie, K., Tran-Nam, B. and M. Walpole, 1996, “A Report into the Incremental Costs of Taxpayer Compliance”, ATO, Sydney; and Niemirowski et al at note 11 reported response rates of 50.1% and 34.6% respectively.
21 TaxPack was first introduced for the year ended 30 June 1990. More recent developments by the ATO include an Internet facility introduced from the year ended 30 June 2000 for personal taxpayers to complete and lodge their income tax returns. Approximately 30,000 individual taxpayers lodged their 2000 income tax return in this manner, with this figure increasing to over 110,000 in 2001 (ATO Media Release – Nat 01/68 available at: http://www.ato.gov.au/content.asp?doc=/content/corporate/mr200168.htm accessed 080502. All respondents in the survey indicated that they had lodged a paper-based return.
22 Long, S, and J. Swingen, 1987, “An Approach to the Measurement of Tax Law Complexity”, The Journal of the American Taxation Association, Spring at 22-36. In addition, the survey included questions on other potential causes of complexity (such as personal circumstances), but they were found to be unnecessary.
forms (the format or instructions were confusing).

The most common problem reported was in understanding the instructions in TaxPack. In terms of level of difficulty, the more serious problems were attributed to the rate of change in tax rules, understanding the instructions in TaxPack and other written material provided by the ATO, and the time taken to complete the return form. In terms of respondents’ three most difficult problems, TaxPack was ranked the most common major problem by more than double any other. Complexity of rules and understanding other written material from the ATO were ranked as the next two most difficult problems. The time taken to complete the tax return and the rate of change followed. The use of technical language did cause problems, but this was ranked as being a minor concern.

It was concluded that the principal cause of complexity, in this context, was ambiguity. To address this cause, the ATO had included ever increasing amounts of detail in material prepared for the use of personal taxpayers. Due to both the volume of material and its rate of change, taxpayers found that understanding the information provided took up too much time. The most constructive means for addressing ambiguity appeared to be the development of clear and simple rules, with less detail and less exceptions. This should reduce both uncertainty and the time taken for personal taxpayers to complete their returns.

It was recognised that the relationship between complexity and compliance behaviour could not be adequately addressed by the survey. However, it appeared reasonable to expect that unintentional noncompliance could result where respondents had encountered problems in completing their returns, depending to some extent on the means by which these problems were resolved. This potential for unintentional noncompliance as a result of complexity was apparent when it was found that two-thirds of those respondents who had encountered problems did not resolve them by either contacting the ATO or using ATO instructional material. Instead, they chose to ask family members, friends or colleagues for advice, or to rely upon the previous year’s return. On this basis it appeared that there was scope for the ATO to improve personal taxpayers’ perception of its role and increase the uptake of its service function, which in turn, could perceivably reduce the incidence of unintentional noncompliance.

The use of a tax agent clearly imposes a monetary compliance cost, apart from psychological and time costs that are incurred by all taxpayers irrespective of who completed their return. Of these (n = 316), 54 per cent indicated that they had never previously completed their own return. Respondents’ most common reason for not completing their own return was that they believed the other person to be more qualified or experienced (55 per cent), followed by the belief that the task was too complicated (30 per cent). For those respondents who had lodged their returns in the past but no longer did so, the main reasons given were that the tax system had become too complicated (46 per cent) and that there had been too many changes (22 per cent). A very small minority (less than 5 per cent) of respondents who used a tax agent or other third party indicated that they did so in order to maximise their refund. It appeared that complexity had resulted in personal taxpayers who had previously completed their own return now no longer doing so, and further, it had undermined the confidence of those who had never completed their own tax return.

The use of a tax agent clearly imposes a monetary compliance cost, apart from psychological and time costs that are incurred by all taxpayers irrespective of who completed their return. It is argued that the total compliance cost is a reflection of the level of complexity of the income tax system and the obligations it imposes on personal taxpayers. Steps to reduce complexity should result in less stress, less anxiety and less time taken by personal taxpayers in fulfilling their tax obligations. Further, steps taken to empower personal taxpayers to complete their own returns as simply and efficiently as possible (such as education programs or the use of improved processes such as the ATO’s Internet lodgement facility) could reduce compliance costs even further should they reduce the overall reliance on tax agents. It was found that salary and wage earners were more reliant on tax agents than were other income groups, as were respondents who
had not completed a university education or who did not normally speak English at home. Taking these factors into account, the development of well-directed strategies could increase the number of personal taxpayers lodging their own returns, thereby reducing at least their monetary cost of compliance.

On the basis of the quantitative component of the study, it was concluded that complexity for personal taxpayers in Australia did exist, that it could be a cause of unintentional noncompliance given its incidence and the means by which taxpayers resolved it, and that complexity increased compliance costs. However, to be able to develop effective strategies to address these issues, an understanding was required of the influence of the mediating variables on the primary outcomes of complexity, confidence in accuracy of return, commitment to compliance, perception of fairness and the cost of compliance. This was done by conducting chi-square tests at the 95 per cent confidence level and is the subject of the following section.

3.1.2 Mediating influences.

Complexity, as an outcome experienced by personal taxpayers who completed their own returns, and as described in the previous section, was not found to be related to any other mediating variables. That is, complexity affected a wide range of personal taxpayers, rather than an identifiable group based on the demographic variables under consideration. Thus strategies to reduce complexity could not be expected to be more effective by tailoring them to a particular group of personal taxpayers, but rather, broad-based strategies were required.

Respondents were asked to indicate the level of confidence they had in the accuracy of their last return lodged, of which only 40 per cent reported (n = 586) that they believed their return to be 100 per cent accurate. Age and completer type were found to be an influence upon respondents’ confidence in the accuracy of their returns, with respondents who used a tax agent being the most confident.

Of respondents who completed their own return, those in the 65 and over age group reported the highest levels of confidence, presumably as a result of being more experienced in tax matters. Respondents in the under 25 years age group reported the lowest levels of confidence. Thus strategies to improve personal taxpayers’ confidence in their own ability to accurately complete their tax return accurately should be directed at those under 25 years of age, and then those aged between 25 and 65 years of age.

Commitment to compliance as reported by respondents was high, with 94 per cent (n =589) indicating that it was either ‘very important’ or at least ‘fairly important’ to them to have their returns correct. In contrast, only 2 per cent indicated that it was not important to them to have their return correct, with the remaining 4 per cent being neutral.

Level of education and dependant status were both found to be related to commitment to compliance. In terms of level of education, the relationship to commitment to compliance was positive, with university-educated respondents reporting the higher levels of commitment. Respondents without dependants (including spouse) had higher levels of commitment than those with dependants.

The perceived fairness of the Australian income tax system was low, with only 17 per cent of respondents (n = 580) describing it as either ‘fair’ or ‘very fair’. In contrast, 64 per cent described it as either ‘a little unfair’ or ‘very unfair,’ with the balance being neutral. Age was the only mediating variable found to be related to perception of fairness, with respondents aged between 25 and 65 years reporting the stronger negative perceptions, and respondents aged 65 years and over perceiving the fairness of the tax system positively. Respondents under 25 years of age did not perceive the tax system as fair, but were less negative in their perception than were those in the middle age group. Thus strategies to improve personal taxpayers’ perception of fairness appear to be more effective if directed to personal taxpayers aged between 25 and 65 years.
Compliance costs did exist, with respondents indicating that they would, on average, be willing to pay approximately $100 each to have another party complete their return for them. Compliance costs were found to be related to respondents’ age, income type and income level. The highest level of compliance costs reported was related to respondents who were either aged between 25 to 65 years, with high income, or whose main source of income was salary and wages. Thus strategies to reduce personal taxpayers’ compliance costs would appear to be more effective if directed to, for example, salary and wage earners.

While the mediating variables are important in terms of refining target audiences for appropriate strategies where behaviour or outcomes are to be modified, it is necessary to first understand how the primary outcomes themselves may be related to each other. By doing so, the effectiveness and efficiency of such strategies can be maximised in terms of achieving improvements in compliance.

### 3.1.3 Primary influences.

Statistically significant relationships were found to exist between complexity and confidence in accuracy of return; complexity and perception of fairness; commitment to compliance and the cost of compliance. Further, at the 94 per cent confidence level, a statistically significant relationship was evident between complexity and the cost of compliance. It appeared that increasing complexity reduced both taxpayers’ perception of fairness and their confidence in the accuracy of their return, and at the same time, increased their cost of compliance. Taxpayers’ high commitment to compliance caused them to have high compliance costs. As this cost of compliance increased, taxpayers’ perception of fairness decreased.

From studying these relationships as a whole, one overall theory was developed in relation to the impact of complexity upon compliance behaviour. It was theorised that complexity and high levels of commitment caused personal taxpayers to experience high levels of compliance costs, which in turn reduced their perception of fairness of the income tax system. As the perception of fairness decreased, there was a decrease in commitment to compliance. If commitment to compliance was not to fall, then the most direct means to ensure that this did not occur was to reduce compliance costs. This could be achieved by reducing complexity, which would have the additional positive effect of increasing the perception of fairness. If taxpayers were committed to compliance (that is, had formed the intention to comply), then provided that other external factors (including complexity) did not affect them, then the outcome should be ‘intentionally compliant’ taxpayers. This overall theory is presented at Figure 2.

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23 Weighted average responses were used based on the three types of completers.
24 For the purposes of this study, the income thresholds used corresponded to the marginal tax thresholds for the year: low (<$20,701), middle (>-$20,700 but <$50,001) and high (>-$50,000).
One obvious limitation of this model is that there may be other factors beyond the scope of this study that could be influential. For example, commitment to compliance could also be affected by taxpayers’ personal circumstances and attitudes, the existence or otherwise of opportunities for evasion, and the effectiveness of the enforcement regime. Based on responses to the open-ended questions included in the survey, perception of fairness would appear also to be influenced by how wisely taxpayers perceive government to be spending monies raised by taxation.

Another limitation was that the direction of the relationships and the way in which they interacted was an interpretative analysis of the statistical findings, and as such, were unproven. To address this limitation and to learn more about unintentional noncompliance, the qualitative component of the study followed.

3.2 Qualitative component.

The single-unit case study was conducted in accordance with a pre-designed protocol, collecting evidence from multiple sources in a real-life context. The findings from the cases were then to be compared and emerging patterns used to modify theories. At the outset, apart from the overall theory arising from the survey which was used to inform the case study, an additional theory was proposed that complexity caused unintentional noncompliance and that this favoured the tax administration in terms of revenue raised.
There were eight replications of the case study conducted. All replications or cases were conducted independently of each other, with no interaction between subjects, and in the context of the cases completing their income tax return for the year ended 30 June 2001. Of the eight cases, two were males aged under 25 years with high school education and in receipt of low level salary and wage income (referred to hereafter as the “younger” group). Neither had dependents. The remaining cases were all aged between 25 and 65 years, university educated, in receipt of salary and wage income and had dependents (referred to hereafter as the “older” group). Two cases in the older group normally spoke a language other than English at home. With one exception, all cases in the older group were in the high income-level bracket. Cases in this group were of four females and two males.

3.2.1 Case studies in the younger group.

Examining the younger group first, both cases had relied upon TaxPack and both had found it to contain too much information and the language to be confusing. When discussing the process of completion with them, it was readily apparent that their starting point had been the return form itself, rather than reading the instructions in TaxPack. They had scanned the headings and labels in the form and completed the boxes they considered appropriate to them. Both had neglected to answer a question concerning adjustments to their tax-free threshold, which was necessary as both had ceased full-time education for the first time during the financial year. In spite of clear directions on the return form to read specific pages in TaxPack, neither case had done so as they had not realised that this question applied to them. As a result, both cases were unintentionally noncompliant. In addition, one case had been in receipt of a government allowance but had not included this in his tax return, incorrectly believing it to be exempt income.

In both of these cases, there was a limited understanding of the requirements of preparing a tax return and an unwillingness to read through a great deal of material in TaxPack when much of it was considered to be irrelevant to their circumstances. Both wanted to lodge an accurate return. While one was more confident that the other, both believed their returns to be accurate. One had encountered difficulty in completing a compulsory question in the return form (in respect of the medicare surcharge), but had resolved this by leaving the relevant part of the return form blank. Neither had calculated the net tax payable, but both were confident that the ATO would do this correctly. Neither had any knowledge of the likelihood of audit or the level of penalties and both were unsure about the fairness of the tax system.

In terms of the effect of unintentional noncompliance on tax liability, it was found that in the case in receipt of the government allowance, the net effect was neutral given the level of income, while in the other case the subject would have understated the net tax payable by $167.45.

3.2.2 Case studies in the older group.

Of the case studies in the older group, three had encountered problems, of varying levels of difficulty, in completing their 2001 income tax return. In resolving these problems, there had been heavy reliance on the previous year’s tax return. TaxPack, and the advice of both colleagues and family members were also utilised, but to a lesser extent. Where TaxPack had been used to resolve problems, it was apparent that reading had been limited to scanning the introductory

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25 These were volunteers in response to an article in the researcher’s local media. They were interviewed as soon as possible after having completed their tax return and before it was due for lodgement, thus there was a seasonal limitation to the time frame of the case study. Human ethics constraints prohibited the researcher from directly canvassing subjects. While more replications could increase confidence, there is no ideal number of replications in single-unit revelatory studies (Yin, R., 1989, *Case Study Research*, Sage, Newbury Park CA at 56-58).

26 MYOB Tax software was used for the tax calculations. Results in this paper refer to changes to net tax payable and include medicare levy.
paragraphs of the relevant parts, rather than the full text. All cases felt that the income tax system had become more complex over time.

All cases wanted to spend as little time as possible on completing their return, but still were concerned that their return be accurate. Being accurate was more important than the net result of the assessment, which most subjects did not attempt to calculate. It consistently appeared that cases were very committed to compliance, they regarded themselves as “honest” and “truthful” people trying to “do their best”.

Cases in this group had consistently worked from the return form itself, only reading TaxPack when they felt it necessary. Records were accurate and diligently maintained where claims were made. Several cases had incurred expenditure but misplaced receipts or not kept the necessary records, but they had not claimed these amounts as deductions, nor appeared particularly concerned even though this meant they were overpaying their income tax. As one case described, “it isn’t worth the hassle”. It appeared that by avoiding complexity, they managed their compliance cost in terms of stress and time, even though it was at a financial cost to them.

In general, cases found the process of completing their tax return to be tiresome, boring and unproductive. Two had used an agent in the past, but did so no longer because of high cost given that both felt they had done most of the preparatory work. Even so, it was apparent in both cases that they had benefited from this agent-exposure in terms of the methods of claiming deductions and addressing the substantiation requirements.

In terms of perception of fairness, it was apparent that although the cases felt the system was less than fair (to varying degrees), they were prepared (or resigned in some cases) to pay their share. As one case expressed it: “just because I know that there are bank robbers, it doesn’t mean I want to be one too”. There was an acceptance that the tax burden fell heavily on the middle-income salary and wage earner. Paying tax was “inescapable”.

There appeared to be little, if any, fear of being audited, and no cases had any concept of the types of penalties that could be imposed for noncompliance. It appeared that cases preferred to err on the side of caution (to be over-compliant) in completing their returns and, therefore, enforcement activities were not of a concern to them.

In two cases there had arisen an opportunity to evade tax by omitting an item of assessable income which had not been exploited. One had received non-assessable income from a hobby activity, but had declared it as assessable because of uncertainty of its correct treatment. Another had received an amount for services rendered paid from overseas, which may have been untraceable, but chose to declare it as assessable income. While both cases demonstrate the high commitment to compliance, the first case is an example of intentional over-compliance caused by complexity, in that the rules were found to be too difficult to understand. To manage the stress of compliance given the high level of commitment, this case chose to over-comply in response to uncertainty.

In terms of the compliance outcome, all cases in this older group were found to be noncompliant, and in every case, the net outcome benefited the tax administration in terms of revenue collected. Of the six cases, two had instances of intentional noncompliance which were a direct result of complexity. One was the case mentioned previously where the hobby proceeds were declared as assessable. In the other case, it was chosen to claim work-related travel just under the substantiation limits rather than have to satisfy its requirements, even though the case had a diary and could have reconstructed the necessary details. The net tax overpaid as a result of intentional noncompliance was $860.00 and $40.46 respectively.

Five of the six cases had instances of unintentional noncompliance, of which four could be directly attributed to complexity. In the one case where complexity was not a direct cause, a tax agent had been used in the previous year and the fee paid had not been claimed as an allowable
deduction. This oversight by the taxpayer would have resulted in an overpayment of net tax of $160.05.

The four cases where there was evidence of unintentional noncompliance as a result of complexity would all have resulted in an overpayment of net tax. The items (and net tax overpaid) included: not claiming home office expenses ($55.68), not claiming occupation-specific clothing ($98.33), incorrect calculation of capital gain ($1,277.51) and not writing off the cost of borrowing on an investment. In this last case, a claim had been made for attending a work-function which the case erroneously believed to be deductible, resulting in a net overpayment of tax of in this case of $72.75.

There were no cases that were without error, even though all cases were at least 90 per cent confident of the accuracy of their return and four of the eight cases had not experienced any problems in completing their returns. Based on the case studies of both the younger and older groups, there was evidence of complexity giving rise to either unintentional noncompliance or intentional overcompliance, which, in all but one case, favoured the tax administration. In terms of equity as a basic principle of taxation, this could not be regarded as a desirable outcome.

3.3 Reflection on findings from both components.

Comparing and contrasting the findings of both the quantitative and qualitative components is an important aspect of multi-paradigm research in that where areas of convergence emerge, greater confidence can be held in those conclusions. There are a number of important areas where the findings of the two components converge, including the significance and causes of complexity; and the nature of the relationship between complexity and compliance behaviour.

Drawing on both components of the study, the conclusion was drawn that complexity was a significant problem from the perspective of both the taxpayer and the tax administration. For personal taxpayers, complexity caused at least half of those who completed their own returns to experience stress, anxiety and time costs in dealing with the problems it caused. Further, for those who relied upon tax agents to complete their returns, there were also direct monetary costs. Both components of the study confirmed that to cope with complexity, personal taxpayers had adopted strategies such as brokering the task to other more-qualified parties, or, where they continued to undertake the task themselves, to err on the side of caution and overstate their tax liability.

For tax administrators, complexity represented a significant problem in terms of its direct affect on compliance outcomes. From the survey it was apparent that personal taxpayers were not highly confident in the accuracy of their returns, even where completed by a tax agent. This lack of confidence could indicate that there is potential for unintentional errors to be made by all personal taxpayers, not just those who complete their own return. For example, complexity could conceivably give rise to a misunderstanding between taxpayer and tax agent, resulting in an unintentional error in an agent-prepared return. The extent to which this may occur was beyond the scope of the study. However, the case study did support the view that the potential for unintentional noncompliance as a result of complexity did exist, at least in respect of those personal taxpayers who completed their own income tax returns. It is also recognised that the ambiguity created by complexity may provide a shelter for aggressive taxpayers, however, this was not supported by the findings of the case study.

As in all research, there are strengths and weaknesses. The high response rate of the survey and the representativeness of the respondents were strengths of the quantitative component, with non-response bias being a weakness. In respect of the case study, the strengths were internal validity (from pattern matching) and reliability (from the use of a protocol), with the narrow cross-section of cases being a weakness. It is also acknowledged that ideally both components of the research should have been conducted on the same year, but this was not possible in the available time frame.
The causes of complexity were found to be consistent in the two components of the study: personal taxpayers found the voluminous material that they were required to read to generally be beyond what they were prepared to do, it took too much time and effort, in spite of its readability. They wanted straightforward and directly relevant material that would enable them to complete their return accurately and in as short as time as possible.

In terms of the relationships between the primary outcomes that were the subject of the study, there is evidence of considerable convergence, and in particular, the case study does assist in informing the findings from the survey. Firstly, in both components there was evidence of high commitment to compliance, which caused personal taxpayers to experience increased compliance costs. These costs include both non-monetary costs such as time, stress and anxiety; and monetary costs such as paying an agent or by paying more tax than required in the case of self-completed returns. While compliance costs cannot be eliminated, on the grounds of equity and fairness, nor should they be unnecessarily onerous. Based on this research, it appeared that compliance costs for personal taxpayers are currently high and difficult to justify. There was no evidence that a reduction in compliance costs would have a negative impact on commitment to compliance.

Secondly, the effect of complexity was directly related to compliance costs. Increasing complexity caused compliance costs to rise, and decreasing complexity, such as experienced by taxpayers in receipt of government benefits or who did not have work-related deductions to claim, caused compliance costs to fall.

Thirdly, both increasing complexity and increasing compliance costs did have a negative impact on taxpayers’ perception of fairness, which in turn had a negative impact on personal taxpayers’ commitment to compliance. However, commitment to compliance was generally high, and it appeared that other issues, such as government policy on taxation, welfare and spending were more of a negative influence on perception of fairness than was complexity.

In reflecting upon the research problem of how complexity influenced compliance behaviour; it appeared that its influence was either direct or indirect. The model presented at Figure 2 represented the indirect effect of complexity upon commitment to compliance, whereby increasing complexity caused compliance costs to rise and perceptions of fairness to be negatively affected which then reduced personal taxpayers’ commitment to compliance.

The survey did not allow for conclusions to be drawn as to the relationship between commitment to compliance and compliance behaviour, as the later was unknown. However, as a result of the case study, it was observed that as commitment fell, there was a reduction in voluntary intentional compliance (leaving compulsory label fields blank, not lodging the return on time because of frustration with resolving problems). The direct effect of complexity on compliance behaviour was observed in the case study whereby complexity gave rise to unintentional noncompliance and intentional overcompliance: both of which appeared to favour the tax administration in terms of revenue collected. Both the direct and indirect effects of increasing complexity upon compliance behaviour are presented at Figure 3.
Decreasing complexity would directly reduce both intentional overcompliance and unintentional noncompliance. Further, decreasing complexity would indirectly increase intentional compliance by having a positive effect on commitment to compliance as a result of a reduction in compliance costs and increase in the perception of fairness. Thus it follows that there is considerable potential for the tax administration to improve compliance outcomes for personal taxpayers, both directly and indirectly, simply by addressing the causes of complexity.
4. IMPLICATIONS FOR TAX ADMINISTRATIONS.

This concluding section of the paper seeks to formulate strategies for tax administrations to improve taxpayer compliance behaviour, based on the research findings discussed in the preceding sections. In spite of the research being in an Australian context and for a specific type of taxpayer, there are implications of relevance to other taxpayers and regimes.

There are likely to be a number of key aspects that may determine compliance behaviour, some of which will be within the influence of the tax administration, while others, such as taxpayers' financial circumstances, will not. Those aspects that can be directly influenced by the tax administration include enforcement strategies (such as audit rates and penalties); its public persona (such as being a provider of assistance and education) and to some extent, the features and requirements of the tax system itself.

In respect of enforcement strategies, it was not apparent from this research that increasing audit rates or penalties would have a significant impact on compliance behaviour for personal taxpayers given their lack of awareness and conscious concern. However, given the frequently expressed comment in the survey that others did not pay their fair share of tax, it would appear that some level of enforcement is considered desirable by taxpayers and does have a positive impact on their perception of fairness and commitment to compliance.

In respect of the public image that the ATO seeks to project, it has developed a Taxpayers' Charter and a compliance model that indicate that honest taxpayers and those trying to do the right thing can, in theory, expect a positive and supportive reception. However, both components of this research found that taxpayers were reluctant to seek assistance from the ATO. The reasons for this reluctance were varied and included a lack of confidence in the ability of ATO staff, and an unease about being conspicuous.

This unease did not appear to be driven by lack of trust, but by taxpayers' lack of confidence in their own understanding of the tax system and how this may be perceived by the ATO. Instead, personal taxpayers preferred to either deal with the problem themselves or ask a 'less threatening' third party, both courses of which may lead to higher levels of noncompliance than necessary. It appeared that there was potential for the ATO to further improve its image as a supportive service provider for law-abiding taxpayers. This may be by the provision of local service centres (such as in shopping centres), or by a clear separation of support and enforcement activities within the ATO.

However, how best to service taxpayers required further consideration. The trend has been to produce a great deal of material available via a number of means including paper, facsimile, and electronic. However, it appeared that no matter how well written this material may be, taxpayers only wanted to read the parts that specifically related to them, they wanted to be sure of the answer and they wanted it as quickly as possible. It may be that 'showing' taxpayers how to complete their return may be more effective than expecting them to make sense of the written material. This view was based on the case study component where subjects who had used an agent in the past and received verbal instructions and explanations, and a directly relevant worked example, were better equipped than those who had not.

In terms of systems changes, there were a number of levels to consider including policy formulation and its implementation. In Australia, tax policy was not always complex at the outset, but tended to become complex over time as changes were required (which necessitated

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28 The Taxpayers' Charter is available at the ATO website at http://www.ato.gov.au. It details the rights and obligations of both taxpayers and the ATO. For the ATO compliance model see D'Ascenzo, M., 2000, "Y2K relationships - the ATO and you post 2000", Taxation in Australia, 34(8) at 421-430.
amendments to legislation, public rulings and other explanatory material) generally because of unanticipated effects of the initial policy. Policy that was ill considered and inconstant gave rise to the ambiguity and uncertainty that caused problems for taxpayers. Addressing policy shortcomings created more exceptions to rules, more details, and more change: all of which further increased taxpayers’ compliance costs.

Clear, and consistent tax policy would not only reduce the complexity of the system for taxpayers and their compliance costs, it would improve their perception of the system’s fairness, their commitment to compliance and the level of intentional compliance. Unintentional noncompliance would fall, as would intentional overcompliance. Further, contentious areas of law that may currently shelter more aggressive taxpayers should be reduced as uncertainty is addressed, making taxpayers more accountable for their compliance behaviour. Given that the development of policy is directly within the realm of government and subject to some influence by other arms of the tax authority, it is an area where significant improvements in compliance could be readily achieved if so desired.

Apart from the potential improvement in accurate compliance as a result of clear and consistent tax policy, there are other obvious advantages of having a less complex tax system. For example, its function becomes more evident and this facilitates the appropriate allocation of resources, it is less costly to enforce, more efficient to administer, and its integrity is enhanced as it collects the right amount of tax from each and every taxpayer.

At the implementation level, the research indicates that improvements in compliance can be efficiently and effectively achieved by the ATO addressing the causes of complexity (at least until policy improvements are effective). The challenge for the ATO is to make the process for taxpayers of fulfilling their tax obligations as simple and straightforward as possible so that their commitment to compliance is not compromised.

Strategies to consider here include how to determine the most effective scope and presentation of material to taxpayers that will empower them and affect their engagement. Clearly, the presentation of voluminous, generic, well-written material will not do this, in spite of it being well intended.

Material needs to be succinct and highly relevant to the user. This may mean that there are multiple mini-versions of TaxPack written for specific users, such as first-time school leavers, taxpayers with family, retired taxpayers or those on government benefits, taxpayers with salary and wage income and work-related expenditure, taxpayers who rely on investment income, and so on. This approach could be readily adapted to the completion of electronic returns, where the way in which taxpayers answer certain questions (for example, their occupation or the type of income received) could determine which other questions and information may be relevant, with material not considered relevant not even being viewed.

Further, the requirements placed on taxpayers should not be unreasonable, or made so time consuming that taxpayers are unfairly disadvantaged or else experience onerous compliance costs. For example, the current substantiation requirements for work-related expenditure are tedious, and the research shows that taxpayers feel discouraged from claiming their entitlements as a result. Other more appropriate measures – in the realm of policy - need to be explored to ensure that the basic principles of fairness and equity are achieved, but more simply.

Such a measure, though somewhat extreme, may be that personal taxpayers not be required to lodge an income tax return. Instead, the ATO could prepare a tax assessment for the taxpayer, based on the considerable information available to it already based on taxpayers’ file numbers (TFN) from an extensive range of sources. In the case of personal taxpayers in Australia where income tax is generally withheld at source, there is little opportunity to earn undeclared income. These assessments may require little other than signing of a declaration of acceptance by the taxpayer. Where taxpayers wish to claim deductions, they can have the option of lodging a
return, although this could be negated to some extent by having agreed deductions for various occupations (and avoid the need for substantiation).

Another alternative may be simply to raise the tax-free threshold by $1,000 in lieu of itemised and substantiated work-related deductions for the same amount. Taxpayers who wished to claim work-related expenditure in excess of this amount could still do so provided they met the substantiation requirements.

Where the lodgement of an annual return of income remains a requirement of the tax system, strategies to reduce complexity still exist. For example, every label on the return form should be subject to scrutiny as to its necessity and the value of its contribution. In the case studies, the errors made in respect of the part-year tax-free threshold call its effectiveness into question, at least in respect of school-leavers. On balance, how significant an impact would the omission of such a field have on the integrity of the system? Can the same result be achieved more efficiently?

Further, it may be that information requested in the return form may already be readily available to the tax administration from other reliable sources, thereby making the problems encountered by taxpayers unnecessary. For example, the problems apparent in the case study in respect of income from cash management funds, eligibility for health insurance rebates and liability for medicare surcharge, may have been avoided to some extent by only asking for information not already available to the ATO. This approach, of critical reflection of the necessity of the information requested of (and provided to) taxpayers, is an essential aspect of reducing complexity.

The overall theme thus far is that the tax authority has complexity, a significant cause of noncompliance, right within its immediate grasp. By adopting appropriate strategies to reduce complexity, taxpayers' compliance behaviour can be improved efficiently, effectively and in a timely manner. It will require compromise, but the overall benefits are apparent from the research. Further, these benefits are much more tangible than those that could be derived from strategies to change taxpayers' attitudes, the impact of which upon compliance is neither well understood nor predictable.

At the same time as these direct strategies to reduce complexity and thereby improve compliance, the indirect effect of complexity upon perceptions of fairness and commitment to compliance warrant attention and a number of opportunities are apparent from the research. For example, it was found that personal taxpayers with lower levels of education and with dependants reported lower levels of commitment. While the ATO does not have information on the education levels of its taxpayers, it may be able to rely on extraneous material whereby occupations (which are known to the ATO) can be classified according to an expected education level. These taxpayers could be targeted with programs designed to further raise their level of commitment.

Based on the findings of this research, such programs should be designed to convince these taxpayers of the merits of taxation. For example, that their hard-earned tax dollars are being wisely spent by government; that there is a need for welfare systems in our society and that they should feel positive about their contribution; and that the tax system is being enforced to make sure everyone is paying their fair share. However, it needs to be remembered that overall commitment to compliance was high, thus the need for such programs may not be considered warranted. Even so, it is anticipated that positive programs are more likely to be effective than are negative programs (about enforcement strategies) which may serve to further widen the divide between the ATO and taxpayers.

In conclusion, we all have a responsibility for tax policy. By using our influence wisely, at whatever level it can be exercised, be it as a voter, a taxpayer or an administrator, those in authority need encouragement to commit to the development of clear, sound, long-term tax policies.
policies. History tells us that short-sighted, ill-conceived policies have a limited life span.\textsuperscript{29} However, whilst they continue to appear they create uncertainty and instability at an economic cost to society which is difficult to justify.

Responsible government and administration is essential for the development of clear and sound tax policy that provides the framework of a straightforward tax system. Having an understandable tax system without unnecessary complexity would go a long way to improving the efficiency and effectiveness of tax administration. Further, it would make compliance more readily achievable by committed taxpayers, and at the same time, would engender higher levels of commitment in others: making it a better tax system for all Australians.

\textsuperscript{29} In Australia, two such examples are the training guarantee levy and the savings offset.