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of Tax Compliance Behaviour: The
Moderating Role of Personal Norms**

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International Studies Program
Andrew Young School of Policy Studies
Georgia State University
Atlanta, Georgia 30303
United States of America

Phone: (404) 651-1144
Fax: (404) 651-4449
Email: ispaysps@gsu.edu
Internet: <http://isp-aysps.gsu.edu>

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Procedural justice and the regulation of tax compliance behaviour: The moderating role of personal norms.

Kristina Murphy¹

INTRODUCTION

The aim of regulatory enforcement is to gain future compliance from offenders. At the same time, enforcement practices should not result in the alienation of those they come into contact with. In an area such as taxation, like in many other regulatory contexts, the behaviour being regulated is continuous and fundamental to the long-term health of the community. In such a regulatory context, the goal should therefore be to secure long-term voluntary compliance. This chapter will present an argument for why deterrence-based enforcement strategies might be counter-productive in meeting these goals. Using survey data collected from a group of 652 tax offenders, it will be suggested that a process-based model of regulation—one which places persuasion and fair treatment in the foreground of a regulatory enforcement encounter—offers much promise in the regulation of taxpayer behaviour.²

Deterrence and Tax Compliance

When reviewing the literature on tax compliance, by far the most common approach to explaining taxpayer behaviour is the rational actor approach and its corresponding regulatory strategy of deterrence. The rational actor approach argues that people are motivated entirely by profit-seeking. They assess opportunities and risks and disobey the law when the anticipated fine and probability of being caught are small in relation to the profits to be made through non-compliance (e.g., Allingham & Sandmo, 1972). In the case of the regulation of people's behaviour, the rational choice model focuses upon the ability of expected losses associated with law-breaking to lessen the likelihood that people will break the law (Nagin & Paternoster, 1991). This regulatory model is referred to as the social control model, or deterrence model. According to advocates of this approach, taxpayers should be deterred from tax non-compliance when they perceive the chance that their non-compliance will be detected to be high and the consequences and penalties to be severe and costly.

The deterrence model has tended to dominate the formulation of public policy in areas as diverse as criminal justice, welfare policy, and taxation. But does it work? Indeed, some research does support the suggestion that variations in the perceived certainty and severity of punishment do shape people's compliance with the law (see

¹ Faculty of Arts, Deakin University, Waurn Ponds, Victoria 3217, Australia. t.murphy@deakin.edu.au. The present research was supported by the Australian Research Council (Grant Number: DP0666337).

² Through the introduction of the Taxpayer Compliance Model, the Australian Taxation Office (ATO) has recently recognised the value of such an approach for regulating taxpayers. While a discussion of this model and its application to tax administration is beyond the scope of this chapter, readers interested in the ATO's new approach to taxpayer enforcement are directed to Braithwaite (2003a; 2003b; 2007); Job, Stout & Smith (2007); and Murphy (2004a).

Grasmick & Bursik, 1990), and more specifically their taxpaying behaviour (see Andreoni, Erard & Feinstein, 1998; Fischer, Wartick & Mark, 1992; Franzoni, 2000). For example, evidence of the effects of audit or detection probability has been found using actual taxpayer data (e.g., Witte & Woodbury, 1985), in experimental studies (e.g., Alm, McClelland & Schulze, 1992; Alm, Sanchez & DeJuan, 1995), and survey research (e.g., Kinsey & Grasmick, 1993; Varma & Doob, 1998). Similarly, there is evidence for the positive effects of sanction severity on tax compliance (e.g., Alm et al., 1995; Wenzel, 2004a). It should be noted, however, that other studies have yielded inconsistent findings (e.g., Dubin, Graetz & Wilde, 1987; Dubin & Wilde, 1988; Elffers, Weigel & Hessing, 1987; Webley & Halstead, 1986).

Although research supports the basic premise of the deterrence model and its ability to deter people from breaking the law, research also suggests that estimates of the likelihood of being caught and punished have, at best, a minor influence on people's law related behaviour. Some studies suggest that such estimates do not independently influence behaviour when the influence of other factors is considered. For example, in a longitudinal study of juvenile delinquents, Paternoster & Iovanni (1986) found that numerous other factors such as fear of informal sanctions from peers or family also contribute to the deterrence of crime. In the taxation context, Scott and Grasmick (1981) reported survey findings showing that legal sanctions had a greater deterrence effect on tax evasion for respondents who perceived the tax system as unjust and were thus presumably more motivated to evade tax. In an Australian tax study, Wenzel (2004a) also found that perceived deterrence was less effective for respondents who identified strongly as Australians. Wenzel argued that this finding may have been due to 'strong identifiers' being less motivated by individual self-interest than by the collective good. These research findings suggest that compliance with the law may, at best, be only weakly linked to the risks associated with law-breaking behaviours.

Not only has the deterrence model been used to deter would-be non-compliers from breaking the law, but it has also been used as a specific deterrent to those who have already been detected and caught breaking the law. The deterrence model makes the assumption that by handing out harsh punishment and penalties to rule-breakers this will deter them from committing future acts of non-compliance. A growing body of research, however, suggests that deterrence-based enforcement strategies with offenders can sometimes be counterproductive (e.g., Ayres & Braithwaite, 1992; Blumenthal, Christian & Slemrod, 1998; Kagan & Scholz, 1984). In fact, research into reactance has shown that the use of threat and legal authority, particularly when perceived as illegitimate, can produce the opposite behaviour from that sought; these actions are more likely to result in further non-compliance (Brehm & Brehm, 1981; Murphy & Harris, 2007), creative compliance (McBarnet, 2003), criminal behaviour or overt opposition (Fehr & Rokenbach, 2003; Frey, 1997; Kagan & Scholz, 1984; Unnever, Colvin & Cullen, 2004). Kagan and Scholz (1984) further argue that unreasonable behaviour by regulators during an enforcement experience generates resistance to compliance. They suggest that unreasonableness may involve disrespect for citizens, or arbitrary refusal to take their concerns into account in the enforcement process. They suggest that citizen response to such unreasonableness is likely to be weakened respect for compliance with the law.

An analysis of compliance that is patterned on the deterrence model provides an important starting point for thinking about tax compliance. However, although there is evidence to support this regulatory framework, it nonetheless represents only one piece of the tax compliance phenomenon. Behaviour is multifaceted and is influenced by many different factors, including taxpayer disposition toward authority, ethics, morals, norms, and the perceived fairness of the tax system and the way in which enforcement is used. Given the potential problems that deterrence strategies may pose for subsequent compliance behaviour, a number of scholars have therefore suggested that these additional factors need to be considered when managing non-compliance (Braithwaite, 2002; Kagan & Scholz, 1984; Tyler, 2006). These scholars argue that the core motivation of a regulator should be not to punish an evil, but to repair the harm done and to secure future compliance (see also Black, 2001).

A Process-based Model of Regulation

The limits of the deterrence model suggest the importance of developing a broader regulatory model to explain compliance behaviour. One such model has been proposed by Tyler (1990; 2006).³ According to Tyler (2006), people's compliance behaviour is strongly linked to views about justice and injustice. In particular, he suggests that procedural justice plays an important role in peoples' decision to comply with rules and regulations.

Procedural justice concerns the perceived fairness of the procedures involved in decision-making and the perceived treatment one receives from a decision maker during an enforcement experience. The procedural justice literature demonstrates that people's reactions to their personal experiences with authorities are rooted in their evaluations of the fairness of procedures those agencies use to exercise their authority (Lind & Tyler, 1988; Tyler & Blader, 2000). There is empirical evidence to show that people who feel they have been treated in a procedurally fair manner by an authority will be more likely to trust that authority (Murphy, 2004b), and will be more inclined to accept its decisions and follow its directions (Lind & Tyler, 1988; Tyler & DeGoey, 1996). Tyler & Huo (2002) also suggest that procedurally fair regulation also lessens defiance and hostility. In fact, a number of scholars have found that people are more likely to challenge a situation collectively when they believe that the procedures an authority uses are unfair (Greenberg, 1987; Smith & Stalans, 1994; Murphy, 2003).

The procedural justice literature specifically highlights the importance of an authority's trustworthiness, interpersonal respect, and neutrality in its dealings with others (Tyler, 1997). Research has shown that if people believe that an authority has tried to be fair with them, that they have been treated with respect, and that they have been dealt with in an impartial way, then these three factors enhance feelings of fairness. Hence, Tyler & Huo (2002) suggest that instead of relying so heavily on deterrence based strategies, regulators should adopt what they refer to as a process-based model of regulation. According to Tyler & Huo, a more effective regulatory strategy would be to encourage the judgment that a regulator is using fair procedures in exercising their authority and to develop the public's trust in the motives of legal

³ In fact, the principles outlined in Tyler's regulatory model have been incorporated into the ATO's new regulatory enforcement model (see Braithwaite, 2003a; 2003b; 2007; Job, Stout & Smith, 2007; Murphy, 2004a).

authorities. Tyler & Huo refer to this as process-based regulation because such a strategy is based on seeking to gain the cooperation and consent of members of the public through the fair, respectful behaviour of regulatory authorities. Tyler and Huo (2002) show that process-based regulation offers several advantages. As mentioned earlier, it has been shown to lessen defiance and hostility, making it easier for regulators to gain acceptance for their decisions from the public. Second, because people are accepting the decisions of authorities more voluntarily, they are more likely to adhere to those decisions over time. Tyler & Huo suggest that when people unwillingly give way to coercive and deterrence-based strategies, their compliance does not develop from internal motivations. Once the immediate threat of punishment is lessened, people revert to their prior behaviours. This is why they suggest regulators often have to revisit problems and people over and over again to remind them of the possibility of sanctioning.

Procedural Justice and Tax Compliance

Advocates of the deterrence approach would have us believe that economic self-interest factors dominate taxpayers' actions. However, a growing number of research studies have found that procedural justice can in fact be more effective in shaping compliance than instrumental factors such as judgements about gain and losses or about fear of punishment (e.g., Feld & Frey, 2002; Magner, Sobery & Welker 1998; Murphy, 2005a; Wenzel, 2002a, 2006). For example, in a Swiss study, Feld and Frey (2002) presented empirical evidence to suggest that actual tax compliance increased when taxpayers were treated as trustworthy in the first instance by tax authorities; a major principle of procedurally fair regulation. In a study of Australian taxpayers, Wenzel (2002b) also studied the impact of justice perceptions on self-reported tax compliance. Using a survey methodology, Wenzel found that taxpayers reported being more compliant when they thought that they had been treated fairly and respectfully by the Australian Taxation Office (ATO).

More recently, Wenzel (2006) studied the effectiveness of different reminder letters that reminded small business taxpayers about their requirements to lodge their quarterly business activity statements with the ATO. Taxpayers in his study were all non-compliant taxpayers as they had all failed to lodge their business activity statements to the ATO by the required date. Working with the ATO, Wenzel tested three different letters on subsequent lodgement compliance. The first was the ATO's standard reminder letter which made penalties and punishment salient. The other two letters focussed on principles of procedural fairness. The first of these procedural justice letters emphasised consideration and respect for taxpayers (i.e., interpersonal fairness), while at the same time communicating to the taxpayers that they had not fulfilled their taxation obligations under the tax code. The second letter provided taxpayers with information about their obligations and provided justifications for the ATO's decision to pursue them further (i.e., informational justice). Each of the three letters was sent to a random sample of taxpayers (N=2052). It was found that both the informational and interpersonal letter yielded greater lodgement compliance from individuals compared to the standard ATO letter. Importantly, it was also found that fewer complaints and excuses were made to the ATO from taxpayers who received informational and interpersonal letters (Wenzel, 2002a).

Finally, I myself have published research into the effectiveness of procedural justice with taxpayers who have had personal experience with the ATO's enforcement procedures. Using longitudinal survey data collected from 652 tax offenders in 2004, I found that taxpayers who perceived their enforcement experience with the ATO to be procedurally unfair were significantly more likely to report having evaded their taxes again two years later (Murphy, 2005a; see also Murphy, 2003; 2004b). Coupled with the other studies in the procedural justice literature, these tax studies in general suggest that individuals do not react to authorities primarily or exclusively in terms of what they do or do not receive from those authorities. Instead, they react to how they are treated.

THE PRESENT STUDY

The previous section presented empirical evidence to suggest that a process-based model of regulation may prove particularly useful to regulators in the management of tax non-compliance. The findings in general establish a relationship between treating taxpayers with procedural justice and subsequent tax compliance behaviour. However, the conditions under which procedural justice may be more or less effective have not yet received much attention in the taxation literature. For example, is it possible that procedural justice may be more effective in shaping compliance behaviour for some taxpayers than for others? Specifically, would regulatory strategies that rely on procedural justice principles be ineffective for those who hold weak personal norms about obeying the law? If we are to support a process-based model of regulation in the taxation context, we would hope to find that procedural justice can be used effectively with offenders who have little respect for the law.

The moderating role of personal norms?

In addition to being influenced by their judgments about the behaviour of regulatory agencies they encounter during an enforcement experience, people's willingness to comply with the law has also been found to be shaped by their personal norms. If we look at the criminology literature, for example, we can see that one view on why people comply with legal directives is what Skogan and Frydl (2004) refer to as 'substantive morality'. That is, compliance is motivated by personal norms and values. If one's personal norms or values are consistent with the law, cooperation and compliance will be voluntarily extended.

Various studies have demonstrated the important role that personal norms play in predicting taxpaying behaviour. In a classic study conducted by Schwartz and Orleans (1967), for example, it was found that appeals to taxpayers' personal conscience could increase their tax compliance behaviour more so than deterrent threats. A number of other studies produced similar findings of personal norms increasing tax compliance (e.g., Bosco & Mittone, 1997; Erard & Feinstein, 1994; Reckers, Sanders & Roark, 1994; Wenzel, 2004a, 2004b). A particularly interesting pattern of results, however, has shown that personal norms can actually delimit the relevance of deterrence. Wenzel (2004a) found that personal norms of tax honesty were negatively related to self-reported tax evasion and moderated the effects of perceived sanction severity. In other words, Wenzel's findings showed deterrence effects only when personal norms about taxation compliance were weak.

Such findings have important implications about the role that norms might play in the procedural justice-compliance relationship. As suggested by Wenzel (2004a, p549), “deterrence should only be relevant where people’s ethics do not discard non-compliance as one such option altogether.” If this assertion is indeed correct, then we may also expect to see that taxpayers’ personal norms moderate the effect that procedural justice has on compliance behaviour. For a process-based model of regulation to be widely supported, we should also expect to find that procedural justice is effective in shaping the tax behaviour of those who hold questionable norms about paying tax.

The present study builds upon existing research in two ways. It first seeks to replicate and extend those findings which suggest that procedural justice is effective in shaping tax compliance behaviour. Second, it seeks to test whether personal norms moderate the effect of procedural justice on compliance behaviour, as they do for deterrence effects. As is evident from the studies presented above, the relationship between procedural justice and compliance, and between norms and compliance have previously been explored. However, no studies in the taxation context have sought to test the conditions under which procedural justice is more or less effective in nurturing compliance. The present study therefore seeks to examine whether personal norms moderate the effect of procedural justice on self-reported compliance behaviour.

METHOD

Participants and Procedure

The 652 taxpayers who participated in the present study had all been caught and punished by the Australian Taxation Office (ATO) for investing in illegal tax avoidance schemes. All schemes that were used by the taxpayers under study were financially structured in a similar way. Hence, the taxpayers in the present study form a homogenous group in terms of the offence they had been accused of. What makes this case study particularly interesting is the fact that many of the taxpayers who invested in these illegal tax avoidance schemes did so on the advice of their tax agents. Many claimed that they were therefore the victims of aggressive marketing and bad financial advice. This is important because it means that not all those who ‘broke the law’ by investing in these schemes did so for the dominant purpose of cheating the tax system. One would therefore expect there to be a mixture of people in the surveyed group who hold both strong and weak norms about paying tax.

With assistance from the ATO, a nationwide random sample of 1,250 tax offenders was sent a 28-page survey. Taxpayers were invited to participate in a study that was interested in taxpayers’ views of the ATO and their enforcement processes. Taxpayers were informed that their responses would be kept confidential and would not be used against them by the ATO. Non-respondents were followed up over time using an identification number that was affixed to each survey booklet, which was in turn linked to the sample name. A total of four mailings were made, and after a period of approximately three months, a total of 652 useable surveys were received. When adjusting for people who had moved address, had died, or were incapable of completing the survey (N = 146), the response rate was 60%.

Respondents in the final sample were between 25 and 76 years of age ($M = 50.43$, $SD = 9.00$), 83% were male, 46% had received a University education, and their average personal income was approximately AUS\$79,000 ($SD = AUS\$59,000$; at the time of writing the average equated to approximately US\$65,000 or €47,700). Using the limited amount of demographic data provided by the ATO (i.e., state of residence and sex), the sample proved to be representative of the overall scheme offender population ($N = 32,493$).

Measures used in the present study

The survey contained in excess of 200 questions designed to test respondents' attitudes towards the Australian tax system, the ATO and of paying tax. A number of questions were also designed with the aim of assessing investors' self-reported tax compliance behaviour, and their views about their enforcement experience. For the purposes of the present study, however, only those questions relevant to three categories of variables were used: (1) procedural justice, (2) personal norms about taxpaying honesty, and (3) self-reported tax compliance variables. The Appendix lists all items used to construct each scale.

Procedural Justice. The eight-item procedural justice measure was based on previous research conducted by Tyler (1990; 2006). Taxpayers were asked to think back and reflect on the ATO's treatment of them during the enforcement process. The items in the scale were designed to measure perceptions of fair treatment (sample item: 'The ATO tries to be fair when making their decisions'). The factor analysis presented below shows that the eight items loaded strongly onto only one factor. The overall scale was coded in the present study so that those scoring higher on this scale were more likely to see the ATO as having used procedurally fair methods.

Personal Norms. The three-item personal norms scale was based on previous research conducted by Wenzel (2004a, 2004b). The personal norms referred to one's own norms concerning taxpaying honesty (sample item: "Do you think you should honestly declare cash earnings in your tax return?"). Two items of the scale were reverse scored so that those scoring high on this measure were deemed to have strong personal norms that paying tax is the right thing to do.

Tax Compliance. Taxpayers were asked a series of six questions about how they thought their enforcement experience had subsequently affected their taxpaying behaviour (sample item: 'I now look for ways to purposefully cheat the tax system'). All six self-report items were reverse-scored and combined to form the tax compliance scale; those taxpayers scoring higher on this scale were deemed to be more compliant.

Factor analysis

A principle components analysis was conducted to test for the dimensionality of the items, and the eigenvalues (5.08, 3.39, 1.38, 0.83, 0.76) and scree plot of this analysis suggested that three factors should be extracted. Inspection of the rotated factor structure (see Table 1) shows that the three factors extracted in the analysis support the scales that are described in the measures section. Factor 1 comprised

eight items that measured procedural justice, Factor 2 comprised six items that measured tax compliance, and Factor 3 comprised three items that measured personal norms. While one item in Factor 2 ('I no longer declare all my income') was found to cross-load weakly with items in Factor 3, it was decided to retain this item in the tax compliance scale. The reason for this was twofold. First, a separate regression analysis without this single item included produced the same findings and conclusions as the analysis that did include the item (see Table 3). Second, it is perhaps not surprising that a weak cross-loading was apparent between this item and the Factor 3 items. The tax compliance item measures self-reported behaviour to do with declaring cash income. The personal norm items ask participants about their views on paying tax on cash income. Given one set of items measure personal norms, and the other item measures behaviour it could therefore be reasonably argued that the two sets of items are conceptually distinct from one another despite there being a substantial relationship between them.

Table 1. Factor analysis differentiating variables used in the analysis

Item	Factor		
	1	2	3
<u>1. Procedural Justice</u>			
ATO concerned with respecting rights	0.84		
ATO cares about position of taxpayers	0.83		
ATO tries to be fair in decision-making	0.81		
ATO respects individual's rights	0.78		
ATO considers citizens concerns when making decisions	0.77		
ATO generally honest with people	0.73		
ATO gives equal consideration to all	0.72		
ATO gets info. to make informed decisions	0.53		
<u>2. Tax Compliance</u>			
Use tax system in negative way (r)		0.82	
Look for ways to purposefully cheat (r)		0.77	
Now more defiant towards ATO (r)		0.68	
Look for many ways to recoup losses (r)		0.68	
Try to avoid paying as much tax as possible (r)		0.67	
No longer declare all my income (r)		0.63	0.30
<u>3. Personal Norms</u>			
Working for cash is trivial offence (r)			0.77
Should honestly declare cash			0.76
Acceptable to overstate deductions (r)			0.76
Eigenvalues	5.08	3.39	1.38
Explained variance (%)	30	20	8

Note. Principle-components analysis, with varimax rotation. Only factor loadings ≥ 0.30 are displayed.

Before proceeding to discuss the findings of the study, two limitations of the dataset used should first be mentioned. Given the cross-sectional nature of the survey data, it is impossible to make definitive conclusions about the causal direction of any relationships that are found. Accordingly, this study will limit itself to identifying the presence of relationships, which are valuable in themselves, rather than attempting to draw inferences about their direction. It is also important to note that a self-report

measure of tax compliance was used as the measure of repeat offending in the present study. A method that relies on the honesty of the surveyed participants to disclose dishonest behaviour is obviously vulnerable to a challenge to its validity. However, participants were made aware their responses would be kept confidential, and a strong tradition of research in criminology supports the validity of using self-report data in such circumstances (Maxfield & Babbie, 2008; Thornberry & Krohn, 2000).

RESULTS

As noted earlier, this study is interested in assessing the relationship between perceptions of procedural justice, personal norms, and tax compliance behaviour. It is interested in addressing whether a process-based model of regulation might be effective in nurturing compliance for taxpayers who have both strong and weak norms about complying with the law. Specifically, this study is interested in whether personal norms moderate the effect of procedural justice on compliance behaviour. Table 2 presents the means, standard deviations, and alpha reliability coefficients for all scales measured in the present study. It also details the bi-variate correlations between each scale.

Table 2. Means and standard deviations for each scale, and bi-variate correlations among all scales in the study. Figures in parentheses are alpha coefficients.

Variables	Mean	SD	1	2	3
1. Procedural Justice	2.27	0.72	(.89)		
2. Personal Norms	3.94	0.75	-.04	(.69)	
3. Tax Compliance	4.00	0.71	.23***	.34***	(.80)

*p<0.05, **p<0.01, ***p<0.001; all scales measured on a 1 to 5 scale (1 = strongly disagree, 2 = disagree, 3 = neither, 4 = agree, 5 = strongly agree)

Regression Analysis

In order to test whether personal norms moderate the effect of procedural justice on self-reported compliance behaviour a hierarchical regression analysis was performed. All variables were centred prior to analysis. To identify the unique contribution offered by the two predictor variables of interest, ‘personal norms’ was entered separately into the regression model at Step 1, followed by ‘procedural justice’ at Step 2. The ‘procedural justice’ x ‘personal norms’ interaction term was entered into the model at Step 3. Table 3 displays the results for this analysis.

From Step 3 of Table 3 it can be seen that both ‘personal norms’ and ‘procedural justice’ were found to have significant main effects on self-reported ‘tax compliance behaviour’. As expected, these findings indicate that taxpayers who expressed a strong personal norm of tax honesty reported being more compliant, and those who felt they had been treated in a procedurally fair manner by the ATO during their enforcement experience reported being more compliant.

Table 3. Hierarchical regression model for the effect of procedural justice and personal norms on self-reported tax compliance behaviour

Predictor	Step		
	1	2	3
Personal norms	0.34***	0.35***	0.34***
Procedural justice (PJ)		0.25***	0.25***
PJ x personal norms			-0.10**
R ²	0.12	0.18	0.19
R ² change	0.12	0.06	0.01
F change	84.53***	46.72***	7.67**
df	636	635	634

Note. Predictor entries are standardised regression coefficients (β).

** $p < 0.01$; *** $p < 0.001$.

More interestingly, the interaction between procedural justice and personal norms was found to be significant. To probe the meaning of the interaction effect further, simple slope effects of procedural justice over compliance at -1 and +1 standard deviation of personal norms were calculated (Aiken & West, 1991). The simple slope analyses indicate that procedural justice always had a significant influence upon compliance levels, but that it had a stronger effect in nurturing tax compliance behaviour among those with weaker personal norms of tax honesty ($\beta = 0.35$, $p < 0.001$). Procedural justice significantly affected compliance levels in a positive way for those with strong personal norms ($\beta = 0.15$, $p < 0.01$), but the influence was weaker. These results reveal that personal norms do moderate the effect of procedural justice on compliance behaviour. For a graphical depiction of this interaction effect see Figure 1.

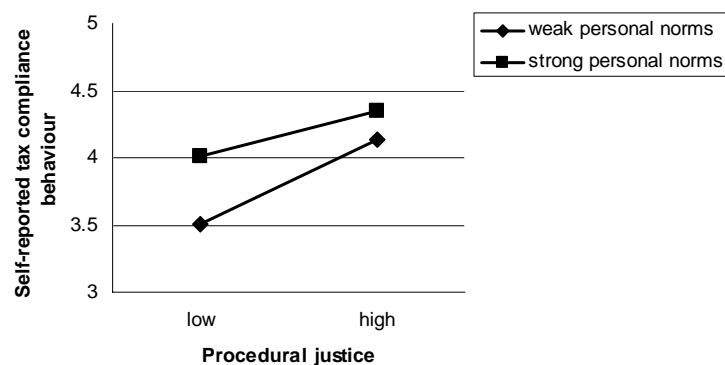


Figure 1. Interaction between procedural justice and personal norms on self-reported tax compliance behaviour. Note: The standardised simple slopes are depicted here for -1 and +1 standard deviations of each predictor variable.

DISCUSSION

As discussed in the introduction to this chapter, taxation researchers have found that regulatory enforcement strategies that rely solely on deterrence principles can be used to deter people from breaking the law. However, a growing body of

research has revealed that deterrence-based enforcement strategies can sometimes generate future resistance to compliance and, under extreme conditions, can encourage game-playing and blatant disrespect for the law (e.g., Ayres & Braithwaite, 1992; Blumenthal et al., 1998; Brehm & Brehm, 1981; Fehr & Rokenbach, 2003; Frey, 1997; Kagan & Scholz, 1984; McBarnet, 2003; Murphy & Harris, 2007; Unnever et al., 2004). Given these limitations, the aim of the present study was to examine whether a process-based model of enforcement—one which relies on treating offenders with procedural justice in the first instance—would be more effective in nurturing long-term voluntary compliance with the spirit of the law.

A number of empirical studies have now demonstrated that taxpayers' perceptions of procedural justice can affect their compliance behaviour; those taxpayers who see a tax authority acting with procedural fairness are more willing to comply with their taxation obligations (e.g., Feld & Frey, 2002; Murphy, 2005a; Wenzel, 2002a, 2006). Such findings point to the value of adopting a process-based enforcement model. Up to now, however, none of this earlier research has attempted to understand the conditions under which procedural justice may be more or less effective in shaping tax compliance behaviour. The present study attempted to rectify this oversight. Specifically, it examined whether taxpayers' personal norms moderated the effect of procedural justice on self-reported compliance behaviour.

The study yielded a couple of interesting and important findings. Using a sample of tax offenders, it was found that procedural justice was related to self-reported tax compliance behaviour, thus supporting prior research. Those taxpayers who were more likely to feel the ATO used procedural justice during their enforcement experience were more likely to report that they had complied with their taxation obligations two years later. As expected, it was also found that norms predicted compliance behaviour. Not surprisingly, taxpayers with stronger norms about taxpaying honesty were more likely to report that they had complied with their tax obligations. Of specific interest to the present study was the significant interaction between perceptions of procedural justice and personal norms on compliance behaviour. It was found that taxpayers with weaker norms about taxpaying honesty were in fact more sensitive to procedural justice effects. Their compliance behaviour was affected more positively by procedurally fair treatment than was the compliance behaviour of taxpayers who held strong personal norms about taxpayer honesty.

The interesting thing about this particular finding is that it mirrors those obtained by Wenzel (2004a) in his examination of the effect that norms play in the relationship between deterrence and compliance. Wenzel found that taxpayers who had weak norms about taxpaying honesty were more strongly affected by the threat of deterrence; they were more likely to indicate they would comply with the law when there was the threat of severe sanctions. In contrast, Wenzel found only weak deterrent effects for those taxpayers who held strong norms about taxpaying honesty. He argued that this was most likely the case because people with strong norms about doing the right thing are likely to comply with the law regardless of what penalties or sanctions may be apparent; deterrence does not become a factor to these people because they would not consider breaking the law to begin with (see also Carroll, 1987; Grasmick & Green, 1980). None of the taxpayers surveyed by Wenzel, however, had been previously punished for tax non-compliance. It was therefore

unclear from Wenzel's study whether offenders are affected by deterrence differently to non-offenders.

In the present study, all taxpayers surveyed had been caught and punished for engaging in tax non-compliance. Here the question is not about how to deter non-compliance in the first place, but how can an authority best regulate offenders to ensure long-term voluntary compliance with the spirit of the law? Many authorities believe that people who do the wrong thing are bound to be nasty pieces of work, and need to be treated like the villains that they are. In other words, when dealing with a 'difficult customer' (i.e., someone with weak norms about doing the right thing), it is generally believed that a hard line and aggressive stance in the first instance will exert power, authority and legitimacy and will therefore be more effective in bringing people into compliance. As Braithwaite (2003b, p35) notes, however, 'from the perspective of the tax authority, part of dealing with an individual's non-compliance is to ensure that it will not happen again, and part is to show the community that compliance standards are high and will be maintained'. Braithwaite argues the challenge for tax administrators is to play a two handed game: to deal with the wrongdoing today, while nurturing consent for tomorrow. What the findings of the present study show is that a process-based model of enforcement may in fact offer some promise in the long term with non-compliant taxpayers, and particularly for those who hold weaker norms about taxpayer honesty. But why should procedural justice be more effective in shaping compliance behaviour among those people who hold weak norms? The following section attempts to provide a possible theoretical explanation for this particular finding.

The virtues of procedural justice: A social distancing framework

There could be a couple of possible explanations for why procedural justice may be more effective in nurturing compliance among tax offenders who hold weak norms about taxpaying honesty. The first explanation for the results is simply a methodological one. As can be seen from Figure 1, compliance levels among those taxpayers who held stronger personal norms about doing the right thing were particularly high, even when they perceived procedural justice to be low. It is therefore possible that a ceiling effect could have masked the positive effects of procedurally fair treatment for this particular group of taxpayer. So rather than procedural justice truly being more effective in changing compliance for those with weak norms, it could be the case that a failure to find a stronger effect in the 'strong personal norms' group was an artefact of a ceiling effect.

Let us assume, however, that the results are not due to a ceiling effect, but are in fact due to some real underlying process. Valerie Braithwaite's (2003b) theory of social distancing offers a possible theoretical explanation for the results. Recent research by Braithwaite (2003b) suggests that people adopt different postures toward authorities and regulators. In the context of taxation, posturing captures the manner in which taxpayers see themselves as they relate to the tax system and the tax authority, and particularly the amount of social distance they wish to place between themselves and the tax authority. Braithwaite (2003b) has shown that taxpayers can adopt five different motivational postures toward a tax authority. These postures are commitment, capitulation, resistance, disengagement and game-playing. Those who adopt a posture of commitment or capitulation place less social distance between

themselves and the regulator and are more inclined to comply with the law. Those who adopt a resistant, disengaged or game-playing posture, in contrast, place greater social distance between themselves and the regulator, and have been shown to be less compliant with the law.

Braithwaite further argues that how taxpayers are treated by a tax authority during an encounter can change their motivational postures in either a positive or negative manner. Tyler (2006) argues that procedurally fair treatment conveys status and communicates to people that they are valued members of society. In fact, other criminological research has shown that regulators are more likely to use harsh punishment and enforcement strategies with people who have lower social standing in the community or who have weaker ties to the regulator (Black, 1976; Grabosky & Braithwaite, 1986; Kruttschnitt, 1980). Harsh and insensitive treatment from an authority during an enforcement process is therefore likely to encourage further psychological distancing between the two sides because taxpayers see themselves as undervalued citizens. Braithwaite argues that if regulators are prepared to first engage in dialogue and fair treatment with those they regulate then this will serve to encourage a more committed posture by the regulatee. This follows that procedurally fair treatment will reduce the social distance between the two sides. In utilising this theoretical approach to explain the findings of the present study, therefore, procedural justice may be particularly effective at nurturing subsequent compliance behaviour among those with weaker taxpaying norms because this group has more opportunity for the social distance gap to be closed; there is more chance that they can move from a posture of disengagement or resistance to one of commitment. People with strong norms about doing the right thing, in contrast, may be more likely to comply with the law regardless of what treatment they receive. Given they are likely to be more committed to the tax system to begin with, procedural justice may be less likely to change their stance toward the tax authority. In other words, there is little room to improve the social distance between the two sides. Although, it should be noted that procedural justice did still have a positive effect on changing compliance for this group.

Empirical evidence to suggest that procedural justice can in fact reduce or change the social distance between a regulatee and regulator comes from an earlier study I conducted (see Murphy, 2005b). Using panel data obtained from the same group of taxpayers studied in the present study, I found that the motivational posture of resistance changed over time if the tax offender had perceived their treatment by the ATO over the previous 2 years to be procedurally fair. Taxpayers were asked to indicate how resistant they were toward the ATO in 2002. They were then asked again in 2004 about their level of resistance toward the ATO. Changes in resistance levels over time were found to be a function of procedural justice; those who felt they received procedural justice became less resistant over time. This adds further support to the suggestion that social distancing theory offers a useful framework in which to explain the results of the present study, although further work in this area is needed to see whether it extends to motivational postures other than resistance.

CONCLUSION

As noted in the introduction to this chapter, the aim of regulatory enforcement is to gain future compliance from offenders. The findings of the present study have

shown that a regulatory enforcement strategy that places persuasion and fair treatment of the taxpayer in the foreground shows much promise in doing just that. In fact, the findings also suggest that a process-based enforcement approach may be particularly effective for those who have weaker respect for the law than for those who have a strong commitment to do the right thing.

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APPENDIX

Contained here is a complete list of the measures used in the analysis of this study. Items denoted with (r) represent items that were reverse scored.

Procedural Justice

- The ATO respects the individual's rights as a citizen
- The ATO is concerned about protecting the average citizen's rights
- The ATO gives equal consideration to the views of all Australians
- The ATO considers the concerns of average citizens when making decisions
- The ATO cares about the position of taxpayers
- The ATO gets the kind of information it needs to make informed decisions
- The ATO tries to be fair when making their decisions
- The ATO is generally honest in the way it deals with people

Personal Norms about Taxpaying Honesty

- Do you think you should honestly declare cash earnings on your tax return?
- Do you think it is acceptable to overstate tax deductions on your tax return? (r)
- Do you think working for cash-in-hand payments without paying tax is a trivial offence? (r)

Tax non-compliance

Below are some statements that describe how your experience may have affected your taxpaying behaviour.

- I now look for ways to purposefully cheat the tax system (r)
- I now use the tax system in a negative way to recoup the financial losses I have incurred (r)
- I no longer declare all of my income (r)
- I am now more defiant towards the ATO (r)
- I now look for many ways to recoup my financial losses (r)
- I now try to avoid paying as much tax as possible (r)