Towards an understanding of the tax practitioner-client role relationship: A role analysis

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Declaration

This thesis is the product of my own work.
All sources used have been acknowledged
within the text and in the references.

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Abstract

Over the years, as tax law has increased in complexity, an increasing number of taxpayers are consulting tax practitioners for help with tax affairs. Yet many tax compliance studies have not incorporated the practitioners' impact on taxpaying behaviour. To bridge the gap in the literature, this thesis investigates the practitioners' and the business taxpayers' roles and relationship using a Tax Practitioner-Client Role Model. This Model is used as a framework for developing a mail survey sent to a sample of business taxpayers and an independent sample of tax practitioners to collect data on their role expectations, experiences and practices, and factors affecting their roles in a tax setting.

The findings show that aggressive tax decisions arise from complex interplay between taxpayer and tax practitioner. Practitioners adapted their decision making to suit cautious or aggressive clients. Their assessment of the likelihood of clients being audited or sanctioned was associated with giving advice that is more conservative or more aggressive, but these effects disappeared when practitioners' own risk propensity was taken into account. Practitioners' firm size was also associated with more cautious or more aggressive advice giving. In comparison, taxpayers' own risk propensity and perceived risk of sanctions predicted their decisions to accept or reject their practitioners' aggressive advice.

While individual characteristics of taxpayers and practitioners were important in making particular decisions, interactions between them took place against a background of shared understandings of roles as well as some misunderstandings. The strongest evidence of shared understandings was found through the dimensions that defined expectations, experiences and practices. Both practitioners and taxpayers conceptualised the other in terms of three dimensions of 'demands' and 'responses': technical proficiency, cautious advice giving, and aggressive advice giving in this order of importance. Both practitioners and taxpayers concurred on the order, but when it came to deciding whether taxpayers received what they expect from their practitioners and whether practitioners delivered on what they perceived to be their clients' expectations, some interesting ambiguities and conflicts emerged.

Taxpayers want all three types of advice, but considered that practitioners fell short of the performance standards expected. Only the technically proficient gap and trust in practitioners affected satisfaction with practitioners' services. This finding implies that a trusting relationship coupled with a competent practitioner is what helps to establish a good practitioner-client relationship.

Tax practitioners perceived themselves differently from the way taxpayers perceived them. They saw themselves as being technically competent, more cautious, and less aggressive in giving tax advice than expected. This finding possibly reflects that practitioners are adept at adapting to their clients, and perhaps even weeding out clients who are not likely to work cooperatively. Qualitative data showed that practitioners are well versed in persuading, listening to, and negotiating with clients. Interactions between a practitioner and client not only affected the ultimate decision made by the client but also helped to resolve role conflict. Interaction is indeed part and parcel of the whole decision making process.

Future research that delves into the dynamics of the practitioner-client relationship might focus on a set of dyads where two specific questions are asked: how is the trust relationship built and maintained from the perspective of each actor and how is the risk taking and uncertainty of each negotiated while preserving this relationship. This thesis was unable to draw on practitioner-client pairs for data collection and had to rely on independent, albeit much larger random samples. Having established the importance of both trust and risk taking in this thesis, the next step is to return to a more limited set of dyads to tease out complexities in the ways in which these variables interact with each other.

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Chapter 1
The Role Demands and Behaviour of Taxpayers and Tax Practitioners

1.1 Background to the study

Tax noncompliance is an area of worldwide concern, as it not only widens the gap between the budgeted and actual tax revenue, but also undermines the government's capacity to achieve other fiscal aims such as economic growth and income redistribution. With a self assessment tax system in place in many countries, the amount of tax revenue collected depends on the compliance behaviour of taxpayers. For those who engage the assistance of a tax practitioner, taxpayers' behaviour could also be influenced by him/her.

Prior studies on tax practitioners, conducted predominantly in the United States (US),[1] indicate that they exert considerable influence on taxpayers in the tax compliance process. By assuming an advisory role, they have a unique opportunity to enhance or dampen taxpayers' propensity to be aggressive (Kaplan, Reckers, West and Boyd 1988; LaRue and Reckers 1989). When aspects of tax law are unambiguous, they tend to adopt the role of "enforcers" but when aspects of the law are ambiguous, they tend to be more "exploiters" (Klepper, Mazur and Nagin 1991).

However, tax practitioners' willingness to exploit the tax law may be driven by various factors such as clients' preference for type of advice, clients' characteristics and practitioners' characteristics (Cruz, Shafer and Strawser 2000; Milliron 1988). For instance, tax practitioners were found to provide aggressive (or conservative) advice to aggressive (or conservative) clients (LaRue and Reckers 1989; Schisler 1994). Such insights elicited from tax practitioners suggest that taxpayers are the instigators of aggressive tax advice. It is interesting to note that, in studies in which the views of taxpayers have been assessed it is reported that they prefer conservative rather than

[1] More recently, several researchers (for example, Braithwaite 2003; Braithwaite 2005; Murphy and Byng 2001; Sakurai and Braithwaite 2003) from the Centre for Tax System Integrity at the Australian National University have conducted a number of studies which relate to tax practitioners' role in taxpaying behaviour.

aggressive advice (Hite and McGill 1992; Sakurai and Braithwaite 2001; Tan 1999). Preference for conservative advice appears to be consistent with the literature, which indicates that one of the main reasons why taxpayers engage a tax practitioner is to file a correct tax return. Ironically, in spite of this motive, some studies show that taxpayers who prefer conservative advice still accept whatever types of advice their practitioner recommends (Tan 1999). Braithwaite (2005), who interviewed tax promoters and advisers in Australia and the US, provides an explanation of how aggressive advice can at times be demand driven and at times supply driven. His data support the view that aggressive advice can be demand driven for boutique shelter products (that is, those that are crafted in response to demand articulated by wealthier clients). However, when they are finessed to the point of being suitable as mass marketed schemes, they have a roller-coaster history. Initially they are supply driven and become demand driven when other taxpayers come to know about these schemes and how well they work. Whether aggressive advice is demand or supply driven, it further affirms the key role practitioners play in taxpaying behaviour.

In addition to analysing taxpayer preferences for conservative or aggressive advice, researchers have investigated characteristics of practitioners and the environments in which they operate. The results, however, are inconclusive as to whether or not for instance, those affiliated with a professional body (such as Certified Public Accountants (CPAs) in the US) are more aggressive than those who are not (Ayres, Jackson and Hite 1989; Cuccia 1994), or whether client importance, probability of audit and severity of penalty have an effect on practitioners' willingness to recommend aggressive tax positions (Bandy, Betancourt and Kelliher 1994; Reckers, Sanders and Wyndelts 1991).

The diversity of these findings implies that not only do the needs or expectations of taxpayers differ but also the types of advice given by practitioners differ. What the literature to date tells us is that aggressive tax advice can be both supply and demand driven. Taxpayers' decisions to adopt aggressive advice and tax practitioners' willingness to provide aggressive advice could further be mediated by a number of other factors. It also appears that both parties can exert influence on each other and that the tax position adopted by the taxpayer is likely to be determined to a considerable degree by the "team play" between taxpayers and their practitioners (Sakurai and Braithwaite 2003). However, the lack of a conceptual framework in many studies and the lack of studies conducted outside the US and Australia make it difficult to draw generalisations about the working relationships between taxpayers and tax practitioners, and the influences on each other of their behaviour. To contribute to the literature in this area, this study focuses on New Zealand taxpayers, tax practitioners, and their roles and relationships.

1.2 Research problem, aims and objectives

In New Zealand (NZ), the absence of regulatory control over who can prepare a tax return allows taxpayers a number of options. They may prepare their tax returns themselves (with or without any help from unpaid third parties), or engage a tax practitioner such as an accountant (who may, or may not, be a Chartered Accountant), a tax lawyer or other types of tax practitioners to assist them. With the complexity of the New Zealand tax system, particularly since the mid-1980s, it is not surprising to find that the number of taxpayers seeking the assistance of tax practitioners has grown (NZ Inland Revenue Department 2001).

In a competitive market, practitioners certainly would want to act in the interests of their clients. Therefore, most practitioners would see their primary role as assisting their clients to manage their taxation affairs in such a way that they pay no more tax than the law requires. How each practitioner arrives at the point where his/her clients 'pay no more tax than the law requires' clearly requires judgement, particularly in cases where the tax law is ambiguous. For instance, some practitioners may consider creative compliance, which is complying with the letter of the law but not its spirit or purpose, as perfectly legitimate whereas some may not (Marshall, Armstrong and Smith 1998; McBarnet 2003).

Practitioners who are members of a professional body (for example, the NZ Law Society or the NZ Institute of Chartered Accountants) have an additional obligation to comply with their institution's code of ethical conduct. This means that they are not to provide any unethical advice. However, most professional organisations' codes of ethics and guidelines serve only as a minimum standard of conduct. As anyone can be a tax practitioner, increased competition may increase pressure on some practitioners to satisfy and maintain the client to the point of even being unethical (Braithwaite 2005; Fisher 1994).[2] Two New Zealand studies conducted by Tooley (1992) and Attwell and Sawyer (2001) showed that tax practitioners' level of ethics was indeed barely satisfactory. However, Braithwaite (2005:13) observes that aggressive tax planning is more of a cyclical phenomenon than constant competition driving down practitioners' ethical standards. The competition recedes as tax authorities ratchet up their enforcement activities. Presumably, at these times, ethical commitment of tax practitioners strengthens as it does in the general population (Braithwaite, Murphy and Reinhart 2007).

All these issues coupled with prior findings from research conducted overseas bring into question the role played by tax practitioners in tax compliance in New Zealand and the demands made by taxpayers on their practitioners. This thesis addresses a set of research questions and issues: What do taxpayers expect of their practitioners? Do they get what they expect? If their expectations are not met, it could mean that they are not communicating their needs clearly to the practitioners, resulting in role ambiguity, or their needs are in conflict with practitioners' ethics or values giving rise to role conflict. Any expectation-experience gap may also have an effect on their satisfaction with, and retention of, their practitioners. If they still retain their practitioners even if they are not getting what they expected, there must be something more that helps to stabilise their relationship. Prior studies have not provided insights into the basis for accepting services that do not entirely meet expectations.

One of the reasons taxpayers engage practitioners is for advice on the tax position they should take when tax law is unclear to them. Where tax law is ambiguous, practitioners are known to exploit tax loopholes to the advantage of their clients, and aggressive reporting is an area of concern to the tax authorities. What will be interesting to discover is whether or not taxpayers will subscribe to their practitioners' aggressive advice. Are there other factors that may influence their decisions? The findings of this study will help to identify which characteristics of taxpayers and features of decision contexts contribute to their decision making.

[2] A recent case of practitioners' unethical behaviour reported in the US involved 19 individuals from KPMG who were charged with conspiracy to defraud the IRS through the use of illegal tax shelters, resulting in at least $2.5 billion in tax being evaded by wealthy individuals (Department of Justice 2005).

A premise that underlies this study is that the taxpayer and tax practitioner form a dyad for decision making. Thus, the following research questions are also raised: What are the practitioners' perceptions of their clients' needs and do they experience role conflict? If so, how do they respond to role conflict? Will practitioners provide aggressive advice to all clients where tax law is ambiguous, or are their recommendations influenced by other factors? Investigating these issues will provide a better understanding of the practitioners' role in their clients' taxpaying behaviour particularly the extent and nature of their influence on taxpaying behaviour.

To address these questions, this thesis aims to investigate the practitioners' and the taxpayers' roles and relationships by focusing on their expectations, experiences, evaluations of, and commitment to their relationships. The empirical focus is not on individual dyads, as interesting as these may be. A study of dyads in the New Zealand context presented two practical and insurmountable problems. First, a study of dyads meant obtaining consent from both a taxpayer and his/her tax practitioner. Second, the questions raised in this study were such that a broad cross-section of both taxpayers and tax practitioners was required. Practically, it was not feasible to attract a sufficiently large sample of dyads. Thus, a sample of taxpayers was drawn and an independent sample of tax practitioners was drawn to address the research questions outlined above.

This decision has implications for how the data collected in this study should be interpreted. The role of tax practitioner is understood as a 'typical practitioner' assessed through taking an average over a sample of practitioners. This is set against the role of a 'typical taxpayer' averaged over a sample of taxpayers. In order to restrict the variability and heterogeneity that can make it difficult to consider meaningfully the 'averaged' roles of tax practitioners and taxpayers, two restrictions are imposed on the study. First, this study investigates the factors that may affect one particular aspect of the tax practitioner-taxpayer roles, that is, giving and accepting aggressive tax advice. Second, the taxpayers under study here are business taxpayers who are not only most likely to seek the services of a tax practitioner but who are also more likely to have the opportunity to benefit from aggressive advice. Focussing on one particular group of taxpayers helps to reduce variability that is attributable to extraneous variables such as 'class of taxpayers'. For this reason, researchers (such as James 2006; Milliron 1988) warn against surveying diverse groups and encourage focus on more specific well defined groups.

An understanding of the roles played by tax practitioners and taxpayers requires an examination of the meaning behind specific roles as well as the behaviour and expectations associated with those roles. As pointed out by Troyer and Younts (1997:697), "roles are not merely labels but rather sets of expectations defining the rights and obligations of persons occupying particular positions in the group."

Since this study concerns roles played by the practitioner and the client in a tax setting, a role theoretic approach is adopted. Accordingly, a Tax Practitioner-Client Role Model, which is grounded in role theory, is developed and used as a framework for analysing the roles of both parties and the factors affecting their roles. The model is adapted from the Role Episode Model (REM) developed by Kahn, Wolfe, Quinn, and Snoek (1964) which revolves around four concepts: role expectations, sent role, received role, and role behaviour. The Tax Practitioner-Client Role Model developed in Chapter 3 takes into account mutual expectations, perceptions and their consequent response and behaviour in relation to aggressive tax advice. It is recognised that expectations and behaviour are moderated by the characteristics of practitioners and clients, the decision context and their interpersonal relations.

1.2.1 Justification for the research

In New Zealand, the self-assessment system relies on taxpayers to take responsibility for reporting and paying the correct amount of tax. Although this approach helps to simplify the government's tax assessment system, it also provides taxpayers with opportunities for aggressive tax minimisation or evasion, as well as unintentional errors. The absence of a regulation system for those who prepare tax returns or give tax planning advice in New Zealand provides opportunities for practitioners to exacerbate all these problems. But most opportunity is presented to the more aggressive players to carve out a niche market in sophisticated tax minimisation (Braithwaite and Braithwaite 2006).

The 2004 Annual Report of the New Zealand Inland Revenue Department (NZ IRD) disclosed that for the year 2003 - 2004, 74% of income tax returns were filed by tax agents on behalf of their clients. In its 2005 Annual Report, further statistics showed that there were around 4,700 tax agents[3] who represented about 1.5 million taxpayers for all, or some, aspects of their taxation in 2004 - 2005 (NZ IRD 2005:31). With such a substantial percentage of taxpayers using the services of tax practitioners, the type of advice provided by the practitioners will be crucially important to the effective operation of the system of self assessment.

If tax practitioners provide taxpayers with aggressive advice which is later challenged by the NZ IRD, the authorities or the Courts may rule either in favour of or against the taxpayers. Aggressive advice, therefore, may not necessarily constitute noncompliance, as it depends on whether one assumes a narrower or wider interpretation. Many scholars, however, have adopted a broader definition of aggressiveness. Braithwaite (2005:16), for instance, defines aggressive tax planning as "a scheme or arrangement put in place with the dominant purpose of avoiding tax." James and Alley (1999) consider noncompliance to encompass tax avoidance where the act of avoiding tax is against the spirit and letter of the law. McBarnet (2003) sees noncompliance as a range of levels of aggressiveness exhibited by taxpayers (in many cases fuelled by practitioners) based on varying degrees of uncertainty about the rules. This type of "creative compliance", if undetected, is considered to be even more destructive of the integrity of the law and therefore poses a much larger problem than outright evasion (Braithwaite and Braithwaite 2006:411; Kirchler 2007).

For these reasons, tax authorities are wary of aggressive advice provided by practitioners to their clients. As such, considerable enforcement resources are utilised by tax authorities to prevent abusive expansion of questionable interpretation (Roth, Scholz and Witte 1989). Indeed, in 2006, the NZ IRD utilised about 850,000 hours in tax audits of small and medium sized enterprises (SMEs) and about 195,000 hours in corporate tax audits (about 825,000 hours and 199,000 hours respectively in 2005). Out of $996 million in audit discrepancies,[4] $247 million related to aggressive tax issues (NZ IRD 2006). Aggressive

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3 As indicated in the NZ IRD website, a tax agent is a person who "prepares annual returns for 10 or more taxpayers and who conducts a professional public practice, or any business that prepares mandatory annual returns." Although registration with the NZ IRD is voluntary, it provides certain benefits such as the option to spread clients' return filing, and access to the NZ IRD's automated services, etc.

4 Audit discrepancies refer to the difference between the tax ascertained as a result of audit activity and that previously returned or ascertained by the taxpayer, plus penalties and interest (NZ IRD Annual Report 2006:20).

tax advice therefore can be a threat to the sustainability of the tax system as the government loses the tax revenue from undetected blatant creative tax schemes.

In addition, the knowledge that tax practitioners can reduce taxes for those who can afford their services may adversely affect the tax commitment of other taxpayers who cannot afford to pay for such services. Prior literature suggests that taxpayers' compliance behaviour may be influenced by their beliefs about the actions of other taxpayers, such as high income taxpayers and corporations, who are perceived as not paying their fair share of taxes[5] (Roth et al. 1989:177).

Business taxpayers (small, medium, or large enterprises) are an important subset of taxpayers, but research relating to their behaviour is limited (James 2006). Their tax affairs are more complicated, and the tax treatment of business income and expenses is more often subject to legal ambiguity as compared to employment income derived by salary or wage earners[6] (Bankman and Karlinsky 2002; Hite, Stock, and Cloyd 1992; Kirchler 2007; Klepper et al. 1991; McBarnet 2003; Slemrod 1985). They are also more likely to seek a tax practitioner to help them with their tax affairs (Christian, Gupta and Lin 1993; Dubin, Graetz, Udell and Wilde 1992; Erard 1993; Klepper et al. 1991; Long and Caudill 1987). Prior research (for example, Hite and McGill 1992; Sakurai and Braithwaite 2003; Schisler 1995) tends to focus on taxpayers in general rather than only on those who engage the services of tax practitioners. As variability attributable to "class of taxpayers" may swamp the more subtle differences associated with roles, this study focused only on business taxpayers who engaged the services of tax practitioners.

The mixed results from prior studies regarding who (that is, tax practitioner or client) is the instigator for aggressive advice further signals a gap in knowledge relating to their respective roles and their working relationships. In most studies (conducted primarily in the US) data were elicited from one particular group only, that is, from either taxpayers or practitioners. To better understand their roles and relationships, it is important to capture

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5 High wealth individuals, no doubt, are another group of taxpayers perceived by the public as not paying their share of tax (Braithwaite, Reinhart, Mearns and Graham 2001; Jackson and Milliron 1986).

6 From the 1999/2000 income year onwards, a huge percentage of these groups were no longer required to file a tax return. This does not rule out the possibility that some who are salary or wage earners may have derived income from other sources. Some of them may still fall under the business group of taxpayers as well.

both the taxpayers' and tax practitioners' perspectives with regard to their expectations, perceptions, and evaluations of tax advisory services provided by practitioners. The development of a Tax Practitioner-Client Role Model, which is grounded in role theory, therefore provides a useful framework for explicating how taxpayers and tax practitioners are likely to affect each other's tax decisions. It further provides a better understanding of what characteristics, contextual factors or interpersonal relations drive tax reporting decisions made by taxpayers and tax practitioners.

In summary, this thesis contributes on two fronts. First, the practitioner-client relationships and roles are examined together with a focus on giving equal weight to both perspectives. While the data for taxpayers and tax practitioners cannot be paired, the sample of taxpayers and the sample of tax practitioners are the best samples that could be practically obtained to represent the views of each side of the tax practitioner-taxpayer relationship. Tan's (1999) preliminary study on New Zealand taxpayers' preference for advice and their willingness to retain a practitioner even if they receive advice at odds with their preference suggests the importance of the tax practitioner-taxpayer working relationship. An examination of the views of both the tax practitioners and business taxpayers provides opportunity to flesh out the dimensions of the working relationship from each perspective and helps to bridge the gap in the tax literature.

Second, the tax setting is New Zealand. With most prior findings on tax practitioners' role originating from studies conducted in the US (and more recently from Australia), the generalisability of the results is limited (Hite, Hasseldine, Al-Khoury, James, Toms and Toumi 2003; Kirchler 2007; Tan 2006). As compared to other countries, New Zealand is particularly interesting as a site for this research because there are relatively fewer institutional constraints on the practice of tax advising. Tax practitioners are not regulated by the government and their services, unlike those offered in many other countries, are geared toward business returns, since many salary and wage earners now do not have to file tax returns.[7]

[7] Generally, one needs to file a return if the income earned is other than salary, wages, interest, dividends, and/or taxable Maori authority distributions.

The findings provide insights into discrepancies between clients' expectations and experience, and their evaluation of practitioners' services. They also reveal the views of practitioners in terms of how they understand their clients' needs and their own professional responsibilities. This study also seeks insights into new dimensions that influence the decision making process. The benefits of this research are therefore not restricted to one particular interest group. Practitioners may benefit through a better understanding of what clients need, and clients may benefit through a better understanding of what practitioners have to offer. Furthermore, if the professional bodies with which tax practitioners are affiliated want to ensure that professional and ethical standards are not threatened by a competitive market pushing practitioners to be more aggressive, then they need to understand the pressures that are operating on practitioners. As the government recognises that tax practitioners have a key role in maintaining an effective tax administration (NZ IRD 2006:27), the findings of this research may further assist them to better understand the motivational factors behind taxpayers and tax practitioners' aggressive postures. Such understanding could help them devise strategies to enhance tax compliance or minimise taxpayers' noncompliance.

1.2.2 Research approach

The research begins by drawing together two bodies of literature: the tax literature that concerns the role of tax practitioners and taxpayers in tax compliance, and the social psychology literature on role concepts. Based on these reviews, a role model of tax practitioners and clients was developed to provide a framework for the study. Several hypotheses were then formulated to test the model.

To achieve the research aim and objectives indicated above, a self-administered mail survey was used to collect the data. The mail survey is one of the most cost effective ways of eliciting the views of a large sample of the general population. As compared to face-to-face interviews, respondents may be more willing to answer sensitive or personal questions, make critical comments, and report less socially acceptable responses in a mailed questionnaire (Moser and Kalton 1997). A mail questionnaire is also likely to suit a population that is reluctant to make appointments for the purposes of survey participation, and who are well versed in completing forms and schedules when it suits them in their own time. A quantitative approach was adopted in this study in order to gauge the relative strengths of association between the many variables implicated in the research question. Quantitative data provides opportunity for statistical modelling and for making generalisations about the population. However, the disadvantage of this method is that it averages individual responses to decision making and action and may conceal individual narratives of how a sequence of events comes about. To redress this disadvantage, both quantitative and qualitative data were collected. This was done by incorporating both closed-ended and open-ended questions in the questionnaire. Responses to the open-ended questions were used to provide further insights and deeper understanding of the practitioners' and taxpayers' perceptions, experiences and behaviour arising from their working relationships and their roles.

Given the interactive nature of a tax service, it was pertinent to examine the views of both parties participating in the exchange to gain a better understanding of their roles and relationships. Accordingly, the questionnaire was sent to a sample of tax practitioners and business taxpayers nationwide. The sample of tax practitioners consists of accountants (Chartered Accountants and non-Chartered Accountants) and lawyers. The sample of business taxpayers consists of those who engaged the services of a tax practitioner.

The Statistical Package for the Social Sciences (SPSS) data analysis program was used for empirically testing the hypotheses with the survey data set. Univariate, bivariate and multivariate analyses were conducted to examine the profile of the respondents and the relationships between variables. Content analysis was used to analyse the responses to the open-ended questions.

1.3 Definitions

1.3.1 Tax Practitioners

In the tax literature, different terms are used to describe a person who is paid to help taxpayers with their tax obligations. The terms used include tax practitioners, tax preparers, tax professionals, professional tax advisers, accountants, tax consultants, tax specialists, tax agents, and lawyers. For the purposes of this thesis, the term tax practitioner is adopted and it refers to all those who are paid by their clients (taxpayers) to assist them with their compliance work or to provide advice on tax planning. They may not necessarily be associated with a professional organisation. Good examples of practitioners in New Zealand are Chartered Accountants (who are members of the NZ Institute of Chartered Accountants - NZICA), accountants (some may be affiliated with the TaxAgents' Institute of New Zealand - TINZ), lawyers (who may, or may not, be members of the New Zealand Law Society - NZLS), and any others who provide tax services for a fee.

1.3.2 Aggressive vs. conservative

The terms 'conservative' and 'aggressive' have a subjective element in them. They refer to the meaning that is attached to law. Moreover, they have become highly value laden terms with connotations of legality associated with 'conservative' and questionable legality associated with 'aggressive.' This heightening of moral sensitivity around the term 'aggressive' has accompanied a growth in the tax avoidance industry globally which has challenged the authority of tax administrators everywhere (Braithwaite and Braithwaite 2006). Its usage in this research context therefore needs clarification.

Interpretations of 'aggressiveness' offered by researchers (such as Hite and McGill 1992; Schisler 1995) tend to reflect consideration of the tax authorities' stance on the position taken, for example, whether there is a reasonable probability that a claim made will be upheld by the tax authorities, or whether it will be easily defended upon a tax audit. It also means that a pro-taxpayers' position is taken on a questionable item.

Another way of interpreting aggressiveness is to adopt the "about as likely as not to be correct" principle specified in the New Zealand Tax Administration Act (TAA) 1994. Based on this principle, there must be about an equal chance (that is, about a 50% chance) of being likely to be correct as there is to be incorrect. The use of the word "about" makes the test less stringent, but the objective interpretation still needs to be close to, or around 50% likely to be correct (NZ IRD 2005). Those who contravene this principle will be penalised – 20% penalty for taking an unacceptable tax position or 100% penalty for an abusive tax position (section 141B TAA 1994). This implies that if the standard is not met, an aggressive stance is taken. In practice, when it is a borderline case, the judgement of "about as likely as not to be correct" can be rather subjective.

To overcome the different interpretations of aggressiveness used in various studies, Carnes, Harwood and Sawyers (1996a:4) define aggressiveness in a relative fashion, that is, those "being more likely than other tax professionals to take pro-taxpayer positions for the same situation" are more aggressive.

In this study the meaning of aggressive which has been adopted is "taking a pro-taxpayer position on a questionable item" where that position is not justified clearly by the facts and relevant professional literature (Cuccia, Hackenbrack and Nelson 1995; Hite and McGill 1992). Whether tax practitioners and taxpayers adopt similar or different interpretations of aggressiveness is another question. The survey data provide an opportunity to examine the perspectives of practitioners and taxpayers on what constitutes aggressiveness in tax advice.

1.3.3 Ambiguous items

Tax law is complex and many rules are subject to an individual's interpretation. Hence, tax authorities and taxpayers or their practitioners could well disagree over the correct treatment of an item or transaction. In this study the term unambiguous items is used to denote those items where the amount that should be reported is legally deterministic, given the facts and circumstances (Klepper et al. 1991:211). In contrast, ambiguous items refer to those where the amount that should be reported is not unequivocally prescribed by statute, regulation, or case law (Klepper et al. 1991) or where there is no shared understanding of what the rule that applies to particular items is (Picciotto 2007). These are the types of items that are most open to creative accounting and aggressive reporting (Andreoni, Erard and Feinstein 1998).

1.3.4 Tax advice

The tax practitioner's literature generally categorises the types of services sought by taxpayers into two main categories, that is, tax compliance and tax advisory/consulting work. Tax compliance work refers to the process of reporting past transactions whereas tax advisory or consultation work involves planning for future transactions. Hence, advice tends to be perceived as relating to consulting work and not compliance work (such as assisting clients in filing a tax return). Such a claim is difficult to sustain on closer analysis. According to the Cambridge Advanced Learner's Dictionary, advice refers to "an opinion which someone offers you about what you should do or how you should act in a particular situation." Therefore, even if practitioners are asked to provide some assistance with the filing of a tax return, they may still provide advice regarding the most favourable interpretation of claims that can be made or the income that is assessable or non-assessable. In other situations, they may provide advice to clients in structuring their transactions in such a way as to minimise tax liability (Dabner 2008). At times, these two functions are intertwined and the same tax practitioner provides both services to the same client, often in the same context (for example, preparing to file a tax return).

The term tax advice used in this study carries a wider connotation than common professional usage. It refers to both the tax practitioner's involvement with compliance and tax advisory and tax planning work.

1.3.5 Taxpayers/clients

The term taxpayer normally refers to a person or organisation that pays taxes. For those who engage a practitioner, they are viewed by practitioners as their clients. For the purpose of this study, the terms clients and taxpayers (those who engage a tax practitioner) are used interchangeably.

1.3.6 Tax compliance vs. noncompliance

Tax compliance describes a taxpayer's willingness to pay tax (James and Alley 2002; Kirchler 2007) and that includes not only the filing of all required returns at the proper time but also that the returns filed accurately report the tax liability in accordance with legislation (Long and Swingen 1991). In contrast, noncompliance describes taxpayers who underreport (or overreport) their taxable income, whether intentionally or unintentionally. Tax evasion, which is a deliberate act to reduce tax liability by illegal means, is clearly a form of noncompliance. Forgetting to declare some income or miscalculating income unintentionally is noncompliance, but does not necessarily qualify as tax evasion (Webley, Robben, Elffers and Hessing 1991).

If willingness to pay tax is extended to mean acting in accordance with the spirit and the letter of tax law and administration without application of any enforcement, then the act of tax avoidance, even though legal, can be considered as noncompliance (James and Alley

1999). Adopting this wider interpretation of noncompliance means that the act of taking an aggressive tax position is also noncompliance. This interpretation of noncompliance is in accord with the different forms of compliance distinguished by McBarnet (2003).

Not everyone may share this wider definition of noncompliance and not all researchers have clarified the interpretation that they have adopted. This lack of clarification, also noted by Richardson and Sawyer (2001) in their review of tax compliance studies, has produced inconsistencies in the research findings of those seeking to uncover the determinants of compliance.

1.4 Delimitations

Clients have a wide range of expectations of their practitioners that can be broadly categorised as either technical or functional, drawing on the marketing literature (Christensen 1992). The technical expectations include for instance, tax savings, reduction of probability of audit and accuracy of tax returns. Functional expectations include efficient service, understanding clients' needs, willingness to help clients, good communication skills, (Christensen 1992) and appointments made easily and quickly (Chang and Bird 1993:22). As there is such a wide array of expectations, it is not possible to consider all of them in this study. Rather, a list of 17 technical and functional expectations for study was drawn from the tax literature.

Prior literature has indicated a number of possible variables which may play a part in shaping attitudes and behaviours of taxpayers and practitioners. Again, it is not possible to consider all the factors in one study. Rather, for this study a conceptual model was developed to prioritise explanation of the giving and receiving of aggressive tax advice.

There are varieties of contexts in which tax advice is given in practice. It was not feasible to consider all possible contexts and all possible tax issues in this study. To have attempted to have done so would have increased the complexity of the questionnaire design as well as lengthening the questionnaire to an unacceptable degree. The ultimate effect of a lengthy questionnaire is that potential participants will be deterred from responding due to its sheer complexity and time required to understand and complete the task. The approach adopted in this study was to define hypothetical contexts for practitioners and taxpayers within the survey instrument. Two hypothetical scenarios were developed for the survey to proxy an expense situation and an income situation.

1.5 Overview of the thesis

Although the extant literature on tax practitioners provided some insights into the reasons for engaging tax practitioners, and the factors affecting the type of advice provided, most of the research has proceeded without an explicit theoretical framework to support the chosen variables. Additionally, many researchers have not considered either the views of both parties, (that is, the practitioners as well as the taxpayers) or their working relationships. The most common concession to recognising the views of the other party has been through reviewing past research and arriving at a generalised statement about the position of the other.

These shortcomings made it difficult to integrate and synthesise empirical research findings to generate a better understanding of the roles and relationships of the practitioners and clients in tax compliance. Drawing from the literature on role theory, this study develops a Tax Practitioner-Client Role Model to provide a better understanding of their working relationships and their roles. Specifically, the expectations, behaviour, and the factors that might drive different aspects of their relationships were examined.

Chapter 2 expands on the background provided in this chapter with a review of the literature that relates to the factors that have the potential to drive taxpayers' compliance behaviour and type of advice provided by tax practitioners. Attention is drawn to the way in which the taxpayers' and tax practitioners' perspectives have been segregated in the literature, with the result that many of the findings present one side of the picture only. It points out also that the inconsistency in findings may be due to a communication gap or miscommunication between clients and their tax practitioners. To achieve a better understanding of the role of tax practitioners in tax compliance, it is argued that there is a need to examine the role behaviour as well as the role demands and expectations of both the client and the practitioner. Both views should be considered due to the interactive nature of the transaction between the tax practitioner and the client.

Chapter 3 provides an overview of role theory and role concepts, and Kahn, Wolfe, Quinn and Snoeks' (1964) Role Episode Model. Based on their model, a theoretical framework by which the tax practitioner and client role and relationship can be understood and analysed is developed.

Chapter 4 details the development of the Tax Practitioner-Client Role Model. The first part discusses and formulates eight research hypotheses from the taxpayers' perspective. The first three hypotheses examine what it takes to establish a stable relationship between the practitioner and client. The next five hypotheses focus on taxpayers' agreement with aggressive advice and the drivers of their agreement. The drivers tested in this study are aggressive advice expectations, personal tax ethics, business tax ethics, risk propensity, and sanction risk perception. The second part develops five research hypotheses from the tax practitioners' perspective. The first hypothesis examines the conflicting demands placed on practitioners, giving rise to role conflict. The next four hypotheses focus on tax practitioners' aggressive advice recommendations and the potential influence of four factors on the aggressiveness of their advice. The four factors considered in this study are practitioners' perception of clients' risk propensity and clients' sanction risk, and practitioners' personal tax ethics and risk propensity.

The procedures for collecting data from taxpayers are described in Chapter 5. This chapter includes a discussion of the sample, also the measurement of concepts and methods of data analysis. The background information about the respondents and the research concepts are also presented in this chapter.

Chapter 6 provides and discusses the results pertaining to the analysis of quantitative data elicited from taxpayers supplemented by qualitative data collected from replies to the open-ended questions. This chapter examines the gap between experiences and expectations for taxpayers, and what this means for the taxpayers' relationship with their practitioners; in particular, what makes for a stable and positive relationship. It also examines what drives taxpayers to agree with practitioners' aggressive advice where the tax law is ambiguous.

Procedures for data collection from tax practitioners are described in Chapter 7. This chapter includes a discussion of the sample, the research concepts that have been measured, and the data analysis. The practitioners' social-demographic profile and the initial psychometric analysis of the measures are also reviewed in this chapter.

Chapter 8 presents the quantitative and qualitative results from the perspective of the tax practitioners. It examines the gap between practitioners' perceptions of clients' expectations and their practice. Their experiences with role conflict and their coping responses to such conflicts are also explored. Chapter 8 then discusses what drives practitioners to provide aggressive advice to their clients where the tax law is ambiguous.

Finally, Chapter 9 provides an overall summary of the results, implications of the findings, limitations of the study and avenues for future research.

Chapter 2
Influences on Taxpayers' Compliance Behaviour and Tax Practitioners' Advice

2.1 Introduction

More than two decades ago, Jackson and Milliron, (1986) in their review of tax compliance research in the US, highlighted the many factors that influence how honest people are when it comes to paying tax. Despite the awareness of practitioners as important 'gatekeepers' to the tax system, in many compliance studies their potential impact on taxpayer compliance decisions had not been considered (Hite and McGill 1992; Roth et al. 1989). Not until the 1980s did interest in this area gain momentum with researchers setting out to examine the practitioners' role. This chapter initially highlights the key empirical findings of factors affecting taxpayer compliance. An overview of the extant literature pertaining to the role of tax practitioners in tax compliance follows. Factors influencing practitioners' advice (conservative or aggressive) are then reviewed.

2.2 Factors affecting taxpayer compliance

Since the 1970s, research conducted on taxpayers' compliance behaviour has flourished and a vast literature on this topic now exists.[8] Moreover, different research paradigms have been adopted by researchers as they set out to investigate the factors that might influence taxpaying behaviour (Kirchler 2007).

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[8] For a comprehensive review of the tax compliance literature see, for example, Andreoni et al. (1998), Jackson and Milliron (1986), Kirchler (2007), Richardson (1998) and Webley et al. (1991). For compliance studies conducted in New Zealand, see Tan and Sawyer (2003).

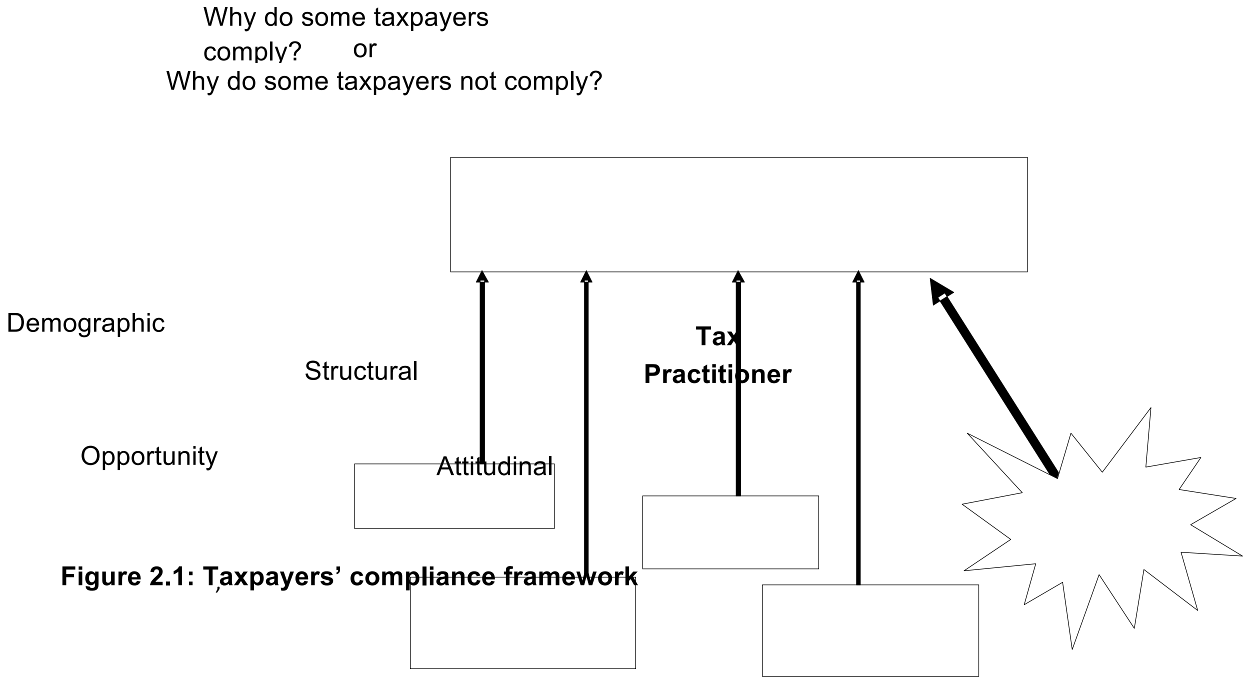

Figure 2.1: Taxpayers' compliance framework

In the first comprehensive review of studies on tax compliance, Jackson and Milliron (1986) identified 14 key variables. These variables were broadly categorised by Fischer, Wartick and Mark (1992) into four main types as shown in Figure 2.1: demographic (for example, age, gender), noncompliance opportunity (for example, income level, education, occupation, and source), structural (for example, complexity, audit probability, tax rates) and attitudinal (for example, ethics, perceived fairness, peer influence). There are certainly many ways of classifying the diverse set of factors affecting tax compliance as can be seen in numerous literature reviews (see for example, Kirchler 2007; Niemirowski, Baldwin and Wearing 2003; Richardson and Sawyer 2001; Webley et al. 1991). In the most recent review by Kirchler (2007), the tax compliance literature is approached from an economic-psychological perspective. This approach can be accommodated within the four main categories of variables shown in Figure 2.1. The overview of the literature on taxpayers' compliance in this chapter follows the framework as displayed in Figure 2.1.[9]

2.2.1 Overview

Numerous studies have been undertaken to test the effect of these different types of variables on tax compliance. In relation to demographic variables, age, as compared to others, has been a relatively consistent predictor (Andreoni et al. 1998). Even so, Jackson

9 Some of the variables are discussed further in Chapter 4.

and Milliron (1986) concluded that the influences of age and other variables such as sex, education, income and occupation were complicated by possible interactions with other variables.

The influence of noncompliance opportunity (for example, education, income level, income source, occupation, tax knowledge) has been a more consistent explanatory factor in noncompliance studies (Kirchler 2007). Certainly, self-employed taxpayers or cash business owners have more opportunities to conceal income or overstate deductions. In comparison, employees whose main source of income is from salaries or wages have fewer, or no, opportunities as their taxes are usually deducted at source. The effect of this variable on compliance is well supported by numerous studies, in which it has been shown that a higher proportion of evaders are indeed self-employed, whereas a higher percentage of wage earners are compliant (Ahmed and Braithwaite 2005; Clotfelter 1983; Hite and McGill 1992; Kirchler 2007; Webley 2004).

Examination of structural factors in tax compliance stems from the classic economic model espoused by Allingham and Sandmo (1972). In this model the taxpayer is treated as a "perfectly amoral, risk-neutral or risk-averse, utility maximising individual who chose to evade tax whenever the expected gain exceeded the cost" (Milliron and Toy 1988:85). It is assumed that individuals weigh the "uncertain benefits of successful evasion against the risk of detection" (Fisher et al. 1992:2). Therefore, variables such as the probability of detection, severity of tax penalties and tax rates are predicted to affect compliance behaviour. This model's prediction stands up well in numerous studies (for example, Clotfelter 1983; Grasmick and Scott 1982; Richardson 1998; Schwartz and Orleans 1967; Tittle 1980; Webley et al. 1991; Witte and Woodbury 1985; Worsham 1996) but not in others (for example, Jackson and Milliron 1986; Slemrod 1985; Spicer and Lundstedt 1976). Of these variables, the most consistent finding is the positive relationship between probability of detection and compliance, although the magnitude of the effect is debatable (Alm, Sanchez and De Juan 1995; Andreoni et al. 1998; Kirchler 2007; Webley 2004). In comparison, there is less evidence of severity of penalties deterring noncompliance (Klepper and Nagin 1989a).

This self-interested economics model has been criticised, particularly by social scientists, for its lack of realism and humanity (Alm et al. 1995; Cullis and Lewis 1997; Kirchler 2007). Although not ruling out the fact that both penalties and audit probabilities have some deterrent effect on taxpayers' compliance behaviour, many researchers have viewed noneconomic factors as important determinants of tax compliance. A number of studies have provided evidence that individuals in many circumstances do not focus only on maximising expected utility (Alm 1991). Rather, taxpayers' decisions between compliance and evasion are affected also by attitudes toward the fiscal system (Spicer and Lundstedt 1976).

Attitudinal factors identified in the compliance literature as having an influence on taxpayers' behaviour include perceptions of fairness, morality, personal norms, social norms, and peer group pressures (see for example, Kirchler 2007; Spicer and Lundstedt 1976; Wenzel 2002). For instance, the effect of fairness or equity on tax compliance has generated considerable interest amongst researchers. Although in some studies it has been established that there is a link between perceptions of fairness and compliance behaviour, some researchers have argued that they may not necessarily be causal factors; rather injustice may be a mere rationalisation for illegal and socially undesirable behaviour (Spicer and Lundstedt 1976). In addition, different taxpayers have different perceptions of fairness. As pointed out by Kirchler (2007), one's perception of fairness can be based on one's perception of tax burden relative to other taxpayers' burdens, an unbalanced exchange relationship between taxpayers and the government, or an evaluation of procedural issues. As a result, studies on the effect of this variable have inconsistent findings as these aspects have not been clearly differentiated (Kirchler 2007; Wenzel 2003).

Empirical support for the importance of taxpayers' concern for social duty or personal responsibility in shaping compliance is more evident (Reckers et al. 1991; Schwartz and Orleans 1967; Wenzel 2002). Some taxpayers pay taxes because they believe it is the right thing to do, irrespective of sanctions (Alm 1991; McGraw and Scholz 1991; Richardson and Sawyer 2001). Individual moral beliefs have been found to be highly significant in tax compliance decisions (Reckers et al. 1991; Torgler and Murphy 2004; Wallschutzky 1984; Wenzel 2002). Spicer and Lundstedt (1976:297) posit that human behaviour in the area of taxation can be affected by internalised norms of role expectations and that these norms may be affected by the behaviour of individuals' reference groups (such as friends, relatives, work associates and so on). Consequently, if taxpayers know that many people in groups important to them are evading taxes, then their commitment to the social norm of tax compliance will be weaker (Kirchler 2007). Wenzel's (2002:551) study comparing personal norms (that is, people's own moral standards, acquired, for instance, through the internalisation of social norms) and social norms (that is, moral standards attributed to a social group) showed that personal internalised norms of tax honesty were negatively related to tax evasion. Moreover, personal internalised norms interacted with sanction severity; sanctions had an effect only when personal internalised norms were weak.

2.2.2 Summary

A significant amount of research contributed by a number of disciplines over at least three decades has provided evidence of multiple determinants of compliance. Psychologists and sociologists have aptly pointed out that the economic model does not fully capture all of the many factors that affect compliance behaviour; others, such as social psychological factors, are also important. Moreover, the social context appears to play an important role in defining when models apply and when they do not (Collins, Milliron and Toy 1990). This is considered to be one explanation for why findings in this area are not readily replicated from one study to another.

Researchers (for example, Braithwaite 2003; Kirchler 2007) have further pointed out that when measuring compliance, attitudes are not necessarily a convincing proxy for behaviour, as evidenced in the studies conducted by Braithwaite (2003), Hessing, Elffers and Weigel (1988) and Weigel, Hessing and Elffers (1987). For example, Braithwaite's study (2003) showed that even though taxpayers have different motivational postures[10] reflecting cooperation and defiance, they were not necessarily as compliant as their postures suggested. Possible reasons for the incongruence between attitudes and behaviour, as offered by her, are that there are circumstances that provide opportunities for noncompliance, tempting people to do (or not do) things that they would not (or would) normally do. In addition, "any single act is shaped by multiple factors, and any small

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10 She identified 5 motivational postures as important in the context of tax compliance. They are commitment, capitulation, resistance, disengagement, and game playing (see Braithwaite 2003).

change in context can be a factor that changes specific behaviour" (Braithwaite 2003:17). These insights further indicate that human behaviour and relationships are indeed complex and there are ample avenues for further research to provide a better understanding of compliance behaviour.

One interesting explanation of attitude-behaviour incongruence in a taxpayer is the influence of the tax practitioner. Indeed, tax practitioners may moderate many of the relationships described above in the tax compliance literature. Many researchers appear to assume that the effect of the factors under consideration is the same irrespective of whether taxpayers file their own tax returns or seek the help of tax practitioners. An underlying assumption made, particularly in the standard tax compliance model, is that all taxpayers are fully informed and understand all relevant aspects of their tax obligations and enforcements (Andreoni et al. 1998). In practice, many are not and those with complicated tax affairs usually rely on the expert knowledge of a tax practitioner.

Tax morale has emerged as one of the most consistent predictors of tax compliance and it appears to be an important factor at the level of tax jurisdictions (Torgler 2007). Tax morale may be low because taxpayers are not well socialised into the taxpaying tradition. It could also be due to their disapproval of government action, or their different set of ethical values that oppose taxpaying (Kohlberg 1976). Interesting questions are: what sustains and nurtures taxpayers' morale, and does the tax practitioner play any role in it? Furthermore, if tax practitioners serve as intermediaries between the taxpayer and the tax authorities, will some factors identified in the literature as influencing taxpaying behaviour wax and wane, depending on how tax practitioners see their role?

Although there is a dearth of literature in which tax practitioners are considered, particularly outside the US, their importance is becoming more accepted and recent researchers have started to explore their roles in taxpaying behaviour (Tan 2006; Tan and Sawyer 2003). In the next section an overview of these developments is provided.

2.3 Literature relating to the role of tax practitioners in tax compliance

The literature relating to the role of tax practitioners in tax compliance is classified into four categories in this section: reasons for using practitioners; preference for type of advice; evaluation of services; and effect of a practitioner on client compliance. Factors affecting the type of advice provided by tax practitioners are considered separately under Section 2.4. As there are more than 50 studies that relate to the role of practitioners in tax compliance, a summary of these studies is provided in Appendix A.[11]

2.3.1 Reasons for using tax practitioners

There are a number of reasons why taxpayers engage tax practitioners. Table 2.1 provides a summary of findings from research conducted to ascertain what motivates taxpayers to hire tax practitioners and the characteristics of this group of taxpayers. A number of studies are either archival studies[12] or surveys conducted in the US. Each source of data provides special insights into the characteristics and factors associated with the demand for tax practitioners' services.

As shown in Table 2.1, the findings from studies carried out by means of surveys are generally consistent with the results from archival studies for the four variables mentioned. Expenditure on professional assistance is positively associated with being older and self-employed, and with having tax obligations that bring into play tax law complexity and time cost (Dubin et al. 1992; Long and Caudill 1987).

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11 The studies considered in Appendix A are not exhaustive as there may be other studies which might have been published in a foreign language or in working papers/theses/dissertation which are not easily accessible.

12 That is, studies in which data derived from official files such as from the Taxpayer Compliance Measurement Program (TCMP) in the US were used.

Table 2.1 Factors associated with the use of tax practitioners

	Archival	Survey
Older	Dubin, Graetz, Udell, & Wilde (1992): +ve	Collins, Milliron & Toy (1990): +ve Slemrod & Sorum (1984): +ve
Self-employed	Long & Caudill (1987): +ve Dubin et al. (1992) : +ve	Christian, Gupta & Lin (1993):+ve Slemrod & Sorum (1984): +ve
Tax law complexity	Long & Caudill (1987): +ve Dubin et al. (1992) : +ve	Collins et al. (1990): +ve Christian et al. (1993): +ve
Time cost	Frischmann & Frees (1999): +ve	Christian et al. (1993): +ve
Income level	Long & Caudill (1987): +ve	Collins et al. (1990): +ve Christian et al. (1993): ns
Audit anxiety	Dubin et al. (1992): +ve	Collins et al. (1990): ns
Tax rates	Long & Caudill (1987): +ve	Christian et al. (1993): ns
Types of income	Long & Caudill (1987): +ve Dubin et al. (1992): +ve	n/a
No. of exemptions or deductions	Dubin et al. (1992): +ve	n/a
Low tax knowledge	Dubin et al. (1992): +ve	n/a
Less educated	n/a	Slemrod & Sorum (1984): +ve
Unmarried	n/a	Slemrod & Sorum (1984):+ve
Tax return prepared correctly	n/a	Collins et al. (1990)# Hite, Stock & Cloyd (1992)# Tan (1999) #
Avoid serious penalties	n/a	Hite et al. (1992)# Tan (1999)#
Pay least tax required	n/a	Collins et al. (1990): +ve Hite et al. (1992)# Tan (1999)#
Reduce chances of being audited	n/a	Hite et al. (1992)# Tan (1999)#
Effort minimisation	n/a	Collins et al. (1990): ns
Social responsibility	n/a	Collins et al. (1990): +ve

+ve = positive effects
ns = no significant effects
# = did not statistically test for association
n/a= not considered in the study

In contrast, studies in which audit anxiety, tax rates, and to a lesser extent income level were examined showed inconsistent results across methods. Other variables examined using only one method, that is either archival or survey, showed that sources of income, number of exemptions, low tax knowledge, complexity of the tax laws and being less educated and unmarried have a positive association with tax practitioner usage by taxpayers (Dubin et al. 1992; Frischmann and Frees 1999; Long and Caudill 1987).

Other survey studies were carried out to provide insight into the relative importance of reasons for using a tax practitioner. For instance, Hite et al. (1992) surveyed small business organisations (SBOs) and found that the most important reason was (i) to have their tax return prepared correctly, followed by (ii) to avoid serious penalties, (iii) to pay the least tax required and (iv) to reduce chances of being audited. Tan's (1999) New Zealand study produced similar findings. Collins et al.'s (1990) study also showed that the vast majority of taxpayers used practitioners to help them file an accurate return, with only 25% stating minimising tax as the primary goal. In addition, Collins et al. (1990) did not find audit anxiety and effort minimisation to be reasons given for use of practitioners.

If taxpayers have their own reasons for engaging a tax practitioner, will they set out to select the type of practitioner who will meet their expectations? Studies suggest that taxpayers do seek out practitioners who match their risk-taking postures (Bankman and Karlinsky 2002; Coyne and Smith 1987;[13] Marshall et al. 1998; Sakurai and Braithwaite 2003). Coyne and Smith (1987) pointed out that those who are risk averse tend to use small to medium sized accounting firms to help them file a safe return. Conversely, clients are more likely to seek a large accounting firm when their primary goal is to reduce their tax bill. Similarly, taxpayers who are interested in taking an aggressive stance within the tax system are more likely to seek practitioners who have demonstrated a willingness to decide ambiguous issues in their clients' favour and have the ability to defend those positions if challenged (Marshall et al. 1998). These findings are in accord with the study by Sakurai and Braithwaite (2003) which indicated that taxpayers choose a tax practitioner who reflects their attitudes toward compliance. Among these ordinary taxpayers, an aggressive tax-planning agent was by far the least desirable option.

The insights gained from these studies are that the reasons for using a tax practitioner seem to gravitate toward safety and economy. It appears that taxpayers do not want to get into trouble with the law and using a practitioner helps them to resolve uncertainty (Blumenthal and Christian 2004; Sakurai and Braithwaite 2003). There could also be taxpayers who feel

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13 Their work is cited in Tomasic and Pentony (1991:243).

that they have a social responsibility. They want to pay the correct amount of tax but do not know how; therefore they consult a tax practitioner. By the same token, taxpayers want to pay no more tax than is required and need practitioners to help them to achieve this aim. One could assume that those most inclined to use a practitioner would be those with most to gain on the safety and economy criteria. Once taxpayers know what they want, they set out to look for practitioners that match their needs. From there on, a partnership develops between the dyads, with each exerting some influence over the other in their tax decision making. Understanding practitioner-client working relationships is therefore pertinent to understanding the roles they both play in tax compliance.

2.3.2 Preference for type of advice

Various studies, which indicate that taxpayers are concerned with filing an accurate return, suggest that most taxpayers who seek the assistance of a tax practitioner prefer conservative advice. This preference is well supported in several survey studies (for example, Hite and McGill 1992; Sakurai and Braithwaite 2003; Tan 1999) which showed that taxpayers agreed with conservative advice from a practitioner but disagreed with aggressive advice; thus confirming clients' preference to be on the 'safe' side. On this basis, it would appear that if practitioners provide advice that is inconsistent with their clients' preference, the clients would change their practitioner, at least in the near future. It is interesting that this does not appear to be the case; clients' intentions to retain or dismiss their practitioners were not influenced by their preference for type of advice[14] (Hite and McGill 1992; Tan 1999).

This finding signals taxpayers' dependence or reliance on their practitioners for tax advice. Taxpayers perhaps placed a lot of trust in their practitioners as they are deemed the tax experts. Therefore, even though taxpayers know their preferences, they are prepared to be swayed by their practitioners' advice. This body of literature raises the question of who instigates and who prevails in the advice that guides action. Murphy's (2001) interviews with a small group of scheme investors revealed that most of them indicated that a tax expert approached them to invest in tax schemes. This insight appears to point to

[14] Hite and McGill's (1992) sample consisted of those who engaged (58%) and those who did not engage (42%) a paid preparer. When they focused on only those who usually engaged a paid preparer, their results implied that taxpayers tended to be loyal to their preparer regardless of the type of advice received.

practitioners as the instigators of aggressive tax reporting. However, it is not clear whether these investors were pursuing their practitioners to look at ways to minimise tax, and therefore indirectly elicited these offers of advice. Murphy and Byng's (2001) findings that 44% of investors did not blame their practitioners for amended tax returns implied that they could be aware of the risks involved and were willing to take the risks. On the other hand, those who placed at least some blame on their practitioners perhaps might not have realised the risk. Possibly the promoters or their practitioners failed to explain the potential risk to them.

It is also interesting to note that the results from studies in which the opinions of practitioners regarding the instigation of aggressive advice have been sought suggest otherwise (Ayres et al. 1989; Braithwaite 2005; Erard 1993; Hite et al. 1992; Kaplan et al. 1988; Schisler 1995). Accountants generally perceived that their clients' proposals for tax alteration, tax fraud or tax evasion were the major ethical problems confronting them (Finn, Chonko and Hunt 1988; Leung and Cooper 2005; Sandford and Dean 1972).

Taken together, these findings suggest that drawing information from one perspective, that is that of either the taxpayer or the tax practitioner, fails to provide a complete picture of the working relationship between the dyads in a tax setting. As indicated earlier, it is likely that both parties have some influence over each other in their tax-related decision making.

2.3.3 Evaluation of tax services

Of relevance to the discussion of how taxpayers use practitioners is the issue of how they view the services that practitioners provide. Not many researchers have examined this issue. Christensen's study (1992) on taxpayers (and practitioners) reported that a client's satisfaction with a service was more dependent on what s/he actually received (advice or a completed tax return) than the way in which the service was delivered. In particular, taxpayers liked their practitioners to provide more tax planning assistance. Her findings further showed that taxpayers expressed disappointment in practitioners who did not adequately understand their individual needs with regard to tax services. Overall, clients had higher service expectations than their practitioners were willing or able to offer. In another study, conducted by Chang and Bird (1993), the tax service quality of tax practitioner was examined. Their findings showed a significant gap (that is, expectation-experience gap) between what clients expected to save by using an adviser and what they felt their adviser actually helped them to save.

One implication of these expectation-experience gaps is that clients are not satisfied with the advice they received from their practitioners, particularly with regard to saving taxes, and tax planning advice. However, it is not clear whether those who were dissatisfied with the service in fact changed practitioners or would change practitioners in the future.

It is also not clear from these studies whether clients preferred more aggressive reporting than what the practitioners had offered. Sakurai and Braithwaite's (2003) study provided some useful insights in this area. Their findings suggest that there are taxpayers who want to play safe but at the same time are also open to aggressive advice. Taxpayers also liked practitioners who are creative and knowledgeable about aggressive tax planning (Ahmed and Braithwaite 2005). Ultimately, whether or not taxpayers will pursue risky strategies may depend on how much risk they are willing to take.

The mismatch between the expectations of both parties may also be due to the possibility that practitioners may have misapprehended the risk preference of their clients, or misinterpreted their clients' demand for tax minimisation as a preference for illegal or aggressive advice. As such, practitioners may not be willing to compromise their ethical standards to comply with a client's unrealistically aggressive expectations. Clients, on the other hand, may believe that there are legal benefits to be gained which they are missing and they expect their practitioners to know them. Tax practitioners may have picked up these signals, but they may see nothing more that can be done to reduce the tax liability in a legitimate way. There appears to be a more dynamic exchange going on in their working relationship than prior studies have managed to capture.

2.3.4 Effect of practitioners on compliance

Numerous studies have been focused on whether or not the use of a tax practitioner by a taxpayer results in lower compliance. However, the results obtained from these various studies are inconsistent.

Earlier research (such as that by Christian et al. 1994; Erard 1993; Smith and Kinsey 1987) indicated that returns prepared by practitioners had lower tax liabilities, required higher dollar adjustments or exhibited greater noncompliance. Although these findings suggested that taxpayers' use of tax practitioners had a negative effect on tax compliance, it does not indicate who influences whom in their tax decisions. If taxpayers are interested only in filing a correct return, then practitioners could be regarded as instigators of aggressive advice. If taxpayers are also interested in paying the least amount of tax possible, they could instigate aggressive advice from their practitioner. In contrast, other studies (for example, by Hasseldine, Kaplan and Fuller 1994) suggest no significant relationship between the use of a practitioner and tax noncompliance. Tomasic and Pentony (1991) reported that tax practitioners assisted clients in improving compliance with existing laws rather than exploiting grey areas of tax law or devising artificial paper schemes. This view is consistent with the findings of a recent study by Hite and Hasseldine (2003) in which returns prepared by practitioners were found to have fewer tax adjustments than did returns prepared by taxpayers themselves.

There is also the possibility that some taxpayers may not disclose all information about their tax affairs to their practitioners. Under such a circumstance, the practitioners should not be blamed for the incorrect tax return (Book 2009). The qualitative study by Bankman and Karlinsky (2002) is interesting as their study on cash business owners indicated that some admitted to having underreported income themselves, whereas others reported that their practitioners helped to facilitate noncompliance.

In New Zealand, the IRD appears to subscribe to the positive role played by tax practitioners as they recognise the practitioners' ability to educate taxpayers and improve compliance. The Inland Revenue's Compliance Improvement Strategy indicates that, on average, taxpayers represented by an agent are more compliant in meeting their filing obligations than are nonrepresented taxpayers (NZ IRD 2001).

These conflicting results that is, practitioners having a positive, negative or no effect on tax compliance, do not offer much in-depth understanding of the role played by tax practitioners. The literature could be enriched through greater knowledge of the role expectations of taxpayers of their practitioners and the reactions and behaviour of practitioners in response to clients' expectations.

2.3.5 Summary

Research indicates that taxpayers engage a tax practitioner for several reasons, which include (a) helping them resolve uncertainties (b) filing an accurate return and (c) minimising their taxes. It appears that once they have engaged a tax practitioner, they rely very much on his/her advice. However, different taxpayers are bound to have different motivations, expectations and preferences. Preference for type of advice may differ from one taxpayer to another, reflecting the heterogeneity of the taxpaying population. Their preferred type of advice could be influenced by various economic and social psychological factors. The literature to date is not clear as to whether or not taxpayers are the instigators of aggressive advice and whether or not tax practitioners comply with such demands. Also unclear is the extent to which the practitioner influences his/her clients' tax compliance behaviour. Given their reliance on their tax practitioners, practitioners may lead some clients who prefer conservative (or aggressive) advice into accepting aggressive (or conservative) advice. It is also possible that practitioners have incorrectly inferred the preferences of their clients. It is interesting that a mismatch between advice desired and advice received does not necessarily mean that the services of the practitioner will be terminated. There may be other considerations which clients take into account when deciding whether to retain or change their practitioners. Indeed, more research is warranted to provide further insights into roles and expectations of taxpayers and tax practitioners.

2.4 Factors influencing practitioners' type of advice

Research findings leave little doubt that aggressive positions are common among tax practitioners (Ayres et al. 1989; Braithwaite 2005; Kaplan et al. 1988; Roberts 1998). In various studies in which practitioners' willingness to advocate client positions in the grey area have been examined, a number of factors that could potentially influence practitioners' aggressiveness have been identified (Cruz et al. 2000; Milliron 1988). As developed by Milliron (1988), the variables can be classified into three main categories: decision context features, client characteristics and practitioner characteristics. This framework (see Figure 2.2) is adopted in this study to analyse and synthesise the literature on practitioners' advice or recommendations made to clients.[15] Each of these categories is discussed below.

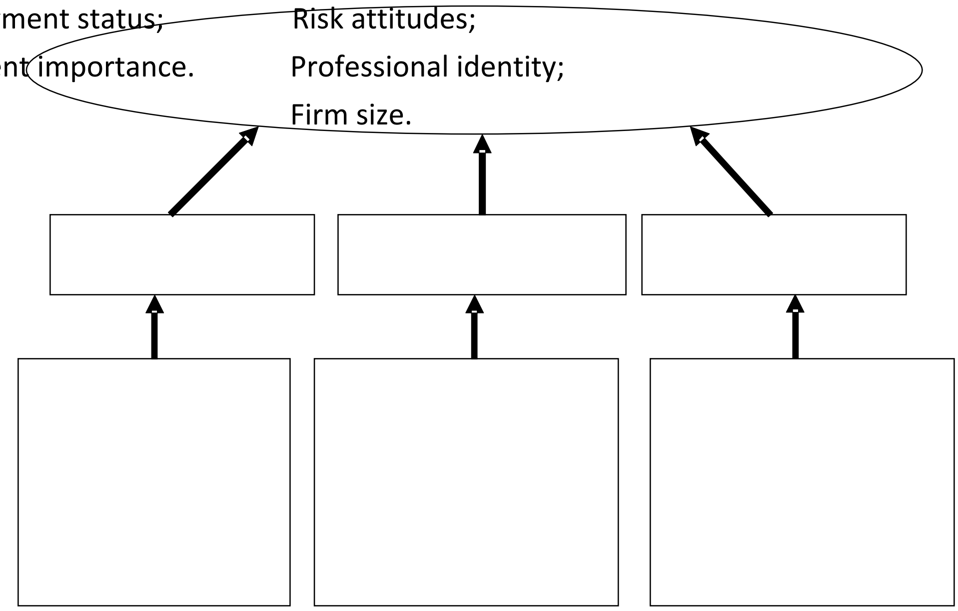

Figure 2.2: Practitioners' type of advice framework

2.4.1 Decision context features

Decision context features are an important influence on the type of advice provided by tax practitioners. Milliron's study (1988) showed that participants from the (then) Big 8 firms rated decision context features to be most influential (45%) in comparison to client-related features (30%) and preparer-related features (25%). The main decision context features are discussed below.

Ambiguity of tax law – Legal factors such as tax law ambiguity can influence a tax practitioner's actions or conduct (Song and Yarbrough 1978). Klepper and Nagin (1989b) produced some evidence that tax practitioners contribute to compliance by enforcing legally clear requirements. Using an economic model to test the relationship, Klepper et al. (1991) confirmed the dual role played by practitioners, that is, they can be "enforcers" as

[15] See also the review on tax accountants' judgment/decision-making research by Roberts (1998).

well as "exploiters" depending on the ambiguity of the tax law. This finding should not be surprising as there is no reason for a responsible tax practitioner to be aggressive when the letter of the law is clear. To be aggressive in such situations will only render his/her clients or him/herself unnecessarily vulnerable to tax penalties.

However, in ambiguous situations, practitioners can advise clients on how to take advantage of ambiguous features of the tax law. As suggested by Klepper and Nagin (1989b:168), the exploitation can benefit the client in two ways. First, unlike unequivocal breaches of legal requirements, a reporting position grounded in legal ambiguity may prevail if challenged. Second, even if the taxpayer is found noncompliant in some respects, the penalty per dollar of noncompliance is likely to be less if the reporting position is based on a credible interpretation of the law. Nowadays, practitioners could even apply for a product ruling on behalf of their client to legitimise the tax planning arrangements. Braithwaite's (2005) interviews with tax practitioners showed that some indeed resort to binding rulings and use them as a resource for structuring arrangements for clients. With these opportunities for avoiding tax, there will always be some taxpayers who are willing to take the risks and will prefer a creative, aggressive practitioner to help them exploit any tax loopholes (Braithwaite 2005; Sakurai and Braithwaite 2003).

Sanction threats - Economic theory has been used to explain an individual's compliant/noncompliant behaviour. As discussed in Section 2.2, the optimal level of evasion, as viewed by economists, is a function of the potential economic benefits (for example, amount of nonreported income or the tax rate) and costs of action (probability of detection and size of penalty). Consequently, a number of studies have been carried out to test the effects of these variables on tax practitioners' aggressive postures. However, just like studies conducted on taxpayers, the effects of sanction threats on tax practitioners[16] have produced mixed results. The study conducted by Madeo, Schepanski and Ueckers (1987) on tax practitioners' reactions to experimentally manipulated income levels, tax rate progressivity, size of penalty and likelihood of detection suggests that the probability of detection exerts the strongest influence. Kaplan et al. (1988) also reported

[16] There are no such penalties that specifically target practitioners in New Zealand. However, if an arrangement is offered, sold, issued, or promoted to 10 or more people in a tax year and it involves an abusive tax position, the promoter will be liable to a promoter's penalty. This penalty was introduced in 2003.

that experimentally manipulated probability of audit (of 50%) registered a significant influence on the type of advice rendered by tax practitioners. LaRue and Reckers (1989), however, found that the perceived likelihood of an IRS audit (of 10% and 25%) had no effect on Certified Public Accountants' (CPA) willingness to encourage aggressive reporting for a real estate tax shelter. The inconsistency of these findings suggests that sanctioning effects do not bear a simple linear relationship to practitioners' compliance. Possibly, audit probability effects kick in only when the risk is perceived as high. Subjective probabilities may have to reach a critical level before they impact on practitioners' reporting decisions.

On the issue of penalties, research indicates that they may, or may not, be an effective deterrent. From interviews of Big 8 tax managers and partners, Milliron (1988) concluded that preparer penalties were one of the important or essential factors influencing tax return preparation. While tax practitioners considered practitioners' penalties very serious, studies (such as those by Jackson et al. 1988; Milliron and Toy 1988) indicate that penalties are for the most part ineffective in altering their behaviour. Results from later studies also suggest that increased penalties imposed on paid practitioners (both CPAs and non-CPAs) had little effect on how aggressively they interpreted ambiguous issues, and CPAs were more conservative only when the threat of penalties was made explicit (Cuccia 1994; Reckers et al. 1991).

Bankman and Karlinsky (2002) argued that preparer penalties are limited as civil penalties are quite modest and the audit rate is far too low. In addition, criminal penalties require proof that practitioners knew that the returns they filed were false; consequently, criminal investigations are rare. Their study on preparers who served misreporting cash businesses showed that most of the preparers' clients were not audited. Neither had they any civil or criminal penalty levied against them. Their view was that a more effective deterrent might involve concentrating on auditing taxpayers and penalising those who are found to be noncompliant.

2.4.2 Client characteristics

A number of studies have shown that practitioners can be heavily influenced by the characteristics of their clients, including client risk attitude, payment or withholding status and importance of client to the practitioner. These factors are discussed below.

Client risk preference/attitudes – An important factor identified as having an influence on tax practitioners' decisions is client risk preference (Milliron 1988). From the tax practitioners' perspective, clients are generally perceived by them to be overly aggressive or are instigators of aggressive advice. An early study by Sandford and Dean (1972) in the UK found that 42 out of the 60 accountants they interviewed believed that clients encouraged them to discover methods of tax minimisation or that clients were very much in favour of tax savings. Similarly, Finn et al. (1988) found from their survey of AICPA[17] members that the most often cited ethical problems confronting the members was client proposals of tax alteration and/or tax fraud. A recent Australian study by Leung and Cooper (2005) indicated that 47% of their respondents who were members of the Australia CPA encountered client proposals for tax evasion, while 50% had encountered client requests to manipulate financial statements. Tooley's (1992) examination of the attitudes of tax practitioners in New Zealand revealed that 71% of the practitioners indicated that their clients were aggressive with the intention of understating income and overstating deductions. This view is confirmed by Attwell and Sawyer (2001) as 52% of their respondents indicated that they encountered client dishonesty.

Previous studies have been focused on practitioners' answers to the question: "Have you encountered tax evasion requests from clients?" These studies, however, did not provide insights into what the practitioners' responses were to such demands. Moreover, there is uncertainty as to the percentage of clients who demanded the help of practitioners in concealing their tax related affairs.

Clients' risk preference has also been linked to practitioners' advice (Cloyd 1995; Cuccia, et al. 1995; Schisler 1994). Practitioners tend to act in empathy with taxpayers by offering different advice to a risk-seeking client and a risk-averse client (LaRue and Reckers 1989, Schisler 1994). For instance, practitioners most likely would recommend

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[17] American Institute of Certified Public Accountants.

aggressive tax positions to aggressive clients (Cloyd 1995) although such actions could be affected by other factors such as the practitioners' perception of audit probability. In contrast, Helleloid (1989) did not find practitioners' decisions to be influenced by clients' attitudes toward risk.

A different picture of tax practitioners' responsiveness emerged from the studies conducted by Duncan et al. (1989) and Pei, Reckers and Wyndelts (1992). In these studies, practitioners gave advice that was more conservative even to aggressive clients, suggesting that they were adopting the role of "enforcers" of tax law. However, in both of these studies highly litigated issues were used. Possibly the practitioners were acting as enforcers to limit negligence concerns, audit probabilities and possible taxpayer penalties. These findings further suggest that there was a mismatch between the type of advice practitioners provided and what their clients were seeking. Other research has shown clients' perceptions of practitioners as understanding their actual levels of aggressiveness. Using a matched-sample, Stephenson (2007) explored the match between clients' perceptions of practitioners' (all from non-Big 4 firms) aggressiveness and practitioners' perceptions of their own aggressiveness. Although her results showed that practitioners were more aggressive than their clients perceived them to be, it is not clear what type of advice clients actually wanted or preferred.

Payment/withholding status - Studies of clients' payment or withholding status addressed the effects of being in a tax due versus a refund position on tax practitioner aggressiveness. According to prospect theory developed by Kahneman and Tversky (1979), decisions are framed in terms of gains and losses. That is, people's attitudes toward risks are different depending on whether it concerns gains or losses. Based on this theory, taxpayers would behave differently depending on whether they are due to receive a refund (which is a gain) or owe tax (which is a loss). Those in a gain situation would behave in a risk-averse manner whereas those in a loss situation would behave in a risk-seeking manner (Schisler 1994). Several studies in which practitioners' aggressiveness has been examined using a prospect theory framework, have produced mixed findings. Sanders and Wyndelts (1989) found that payment status did not affect tax practitioners' recommendations. On the other hand, Duncan et al. (1989) found that clients' payment status had a marginal effect on CPAs' willingness to encourage aggressive reporting. LaRue and Reckers' study (1989) showed no significant main effect for payment status on CPA aggressiveness, although there was a significant interaction between experience, payment status and tax savings. When the opportunity for tax savings was low, less experienced tax practitioners provided more aggressive recommendations for clients who were in a tax due situation. Similarly, Schisler's studies (1994; 1995) produced no significant main effects for withholding status, although there was a significant interaction between withholding status and client risk attitude. Practitioners' aggressive recommendations were not driven by their clients' gain or loss situation perhaps due to the fact that they (the practitioners) were not the ones who were going to be affected financially. However, if practitioners perceived that contradicting clients' wishes (depending on clients' risk preferences) might result in a possible financial loss to them such as losing the clients, then they would recommend more aggressive tax positions with aggressive clients especially those expecting a tax liability. Prospect theory, therefore, is supported under certain conditions only.

It appears from the literature that this variable itself is less likely to have a direct effect on practitioners' advice but instead may interact with other variables to influence advice. In particular, self-employment status may be confounded with prepayment status.

Client importance — Client importance may affect practitioners' willingness to recommend aggressive tax positions (Reckers et al. 1991). Client importance has been operationalised in terms of the size of client firms based on income, turnover or fees received, existing or potential clients, and client tenure. Jackson and Milliron (1987) suggest that practitioners may have different degrees of influence over their clients' decisions. Practitioners may be more likely to represent the government's position where their influence over a client is strongest, that is, clients with lower income and less tax sophistication. However, they may recommend a different reporting position for clients who are in a higher income bracket and are more sophisticated in tax and financial matters. Consistent with these views, Tomasic and Pentony's (1991) interviews of tax practitioners provided evidence that large clients expected them to be more aggressive than did smaller clients. Kinsey (1999) also concluded from her practitioner interviews that the most aggressive firms were associated with the highest income individual taxpayers. In contrast, Bandy et al. (1994) did not find any significant relationship between client importance and the advice given to the client.

Client importance reflects the power that the taxpayer would wield in the tax practitioner–client relationship. Having power, however, is not the same as using power to 'demand' aggressive advice as their tax decisions may be influenced by their practitioners. As practitioners are the tax experts, they are in the position to convince their clients that their advice, conservative or aggressive, is appropriate.

Client tenure is another potential factor in determining the type of advice proffered, as practitioners may lose clients if they do not agree with their preferred tax reporting position. Some studies have shown significant associations between client tenure and tax accounting decisions (Newberry, Reckers and Wyndelts 1993; Milliron 1988). Newberry et al. (1993) found that practitioners provided advice that is more aggressive when they were dealing with existing clients than when dealing with potential new clients. These findings may reflect greater value or importance placed on established clients. Alternatively, it may reflect greater intimacy and trust between practitioner and taxpayer. Established clients are in partnership with their tax practitioners, whereas new clients are not yet in such a relationship.

In the foregoing studies, the focus is on how much one party needs or values the other. It is possible, however, that the observed relationships have a structural base. The aggressive stance taken by practitioners could be due to the fact that influential clients tend to have more convoluted transactions; therefore they have more opportunity to avoid tax and be more aggressive in expecting their practitioners to minimise their tax as much as possible.

2.4.3 Practitioner characteristics

Investigations into the effects of various CPA characteristics on advocacy judgments have focused on demographic characteristics such as gender, age, education, experience level, attitudes, professional identity and size of establishment. Previous studies have generally found weak, or little, effect for demographic characteristics on CPA aggressiveness (for example, Cuccia 1994; Duncan et al. 1989; Schisler 1994). Sanders and Wyndelts (1989) found that male professionals tended to be more aggressive than female professionals but Ayres et al. (1989) and Cuccia (1994) found no such relationship.

The advice given by tax practitioners may also be influenced by the experience of the practitioners themselves. In the case of an ambiguous tax matter, aggressiveness was related to experience levels (Kaplan et al. 1988). For inexperienced tax practitioners, higher audit probability reduced aggressiveness. This was not the case for experienced practitioners. Other studies found little, or no, relation between experience and aggressiveness (Ayres et al. 1989; Cuccia 1994; Duncan et al. 1989).

Cruz et al. (2000) argued that in most of the extant literature a strong economic focus had been adopted as a number of these researchers assumed that the practitioner's judgment is primarily influenced by economic considerations. Although not ruling out the potential influence of economic factors, ethical considerations, such as perceived morality, fairness, cultural acceptability of their actions or their risk propensities may also have an influence on practitioners' judgment (Carnes et al. 1996a; Cruz et al. 2000; LaRue and Reckers 1989; Milliron 1988). In only a few studies has the relationship between practitioners' ethical considerations and the advice offered to clients been addressed. That said, some interesting findings have emerged from research examining how others judged the giving of aggressive advice. For instance, Burns and Kiecker's (1995) investigation of CPAs' attitudes toward unethical actions taken by tax practitioners shows that unethical behaviour was viewed more leniently if the behaviour had favourable consequences for the CPA's firm.

Although prior literature suggests that tax practitioners have encountered ethical problems in discharging their responsibilities, it is not clear how they have resolved such problems.

Professional identity - As any one can practise as a tax practitioner in New Zealand, questions arise as to whether advice differs depending on whether or not practitioners are affiliated with professional organisations. Some studies conducted in the US (Ayres et al. 1989; Cuccia 1994; Erard 1993) have shown a difference – those who were affiliated with a professional organisation (for example, CPA) provided clients with recommendations that were more aggressive than those who were not (for example, non-CPAs or unlicensed practitioners). A recent study by Hite and Hasseldine (2003), on the contrary, found that CPA-prepared returns resulted in fewer audit adjustments than non-CPA returns.

The New Zealand studies also produced mixed results. Although Tooley (1992) found other tax agents to be considerably more disapproving of avoidance measures than both the accountants and the lawyers, he did not find any significant differences in aggressiveness amongst the three groups. In contrast, a later study conducted by Attwell and Sawyer (2001) identified tax agents as the group (compared to other groups such as lawyers or chartered accountants) that least disapproved of tax avoidance.

The mixed results perhaps denote that practitioners are influenced by factors more closely associated with the decision context.

Size of the establishment – Smaller practitioner firms may feel greater pressure to provide aggressive advice to aggressive clients as these clients are important to the firm, and the firm may feel more vulnerable to losing clients (Coyne and Smith 1987). Within the professional class of CPAs in the US, significant differences in reporting recommendations (for example, expenses, capital gains etc.) were found between CPAs employed by large versus small firms (Carnes et al. 1996b; Helleloid 1989; Saunders and Wyndelts 1989). Other findings showed that there were attitudinal differences between CPAs employed by different sized firms (Cuccia 1995) and that those working for the (then) Big 6 firms were more aggressive on tax issues involving high ambiguity (Carnes et al. 1996a). Braithwaite's fieldwork (2005) further confirmed the aggressiveness of the Big 5 accounting firms who were the big players in the corporate tax shelter market. In contrast, Ayres et al. (1989) reported no difference in professionals' judgments across firm type (that is, the (then) Big 8 versus non-Big 8 firms).

2.4.4 Summary

Previous research points to a number of constraints affecting a tax practitioner's degree of aggressiveness in the advice given to clients. Penalties imposed by tax law, audit probabilities, and client characteristics (such as their risk preference or importance) are some of the external factors that may influence their advice. In addition, there is reason to believe that tax practitioners' characteristics (such as professional identity - lawyer, accountant, others) and professional group membership, size of firm and importance of their clientele to the firm, shape levels of aggressiveness in the advice they provide. Finally, the aggressiveness of the advice given to clients could also depend on the number of years of experience the practitioners have and their attitudes towards taxation.

A possible account of the inconsistency in findings is that there may be a communication gap or miscommunication between the client and his/her tax practitioner. Practitioners might have inferred their client's demand for tax minimisation as desiring aggressive advice (Hite and McGill 1992). Clients, on the other hand, might have different risk preferences from others. In Christensen's (1992) finding she alludes to the mismatch between the expectations of both parties. Her results showed that practitioners' beliefs about what the client wanted often differed from what was actually wanted; clients had significantly higher expectations than practitioners realised on nearly every item covered in her survey. The literature also indicates that there appears to be a conflict between what type of advice clients prefer and their tendency to accept whatever advice their practitioner provides. This conflict poses the question of who influences whom. Is it the practitioner who influences his/her client's tax compliance behaviour or the other way round? Alternatively, does the leadership role change hands, with the baton being passed as circumstances change? Another possibility is that taxpayers and tax practitioners are in partnership with both responsible for aggressive tax planning decisions.

2.5 Chapter summary

This chapter draws attention to the way taxpayers' and tax practitioners' perspectives have been segregated in the literature. Nowhere is this more apparent than in the preferred methodologies. The studies reviewed in this chapter can be categorised into three groups based on their chosen sample. In the first category of studies information was elicited from taxpayers only and in the second category of studies information was elicited from tax practitioners only. These two categories of studies therefore each present only one side of the picture. In very few studies has information been elicited from both perspectives at the same time, that is, from both practitioners and taxpayers. Three notable exceptions have been a springboard for the research presented in this thesis. Christensen (1992) in her study discussed in Section 2.3.3 did not use a random sample but had the participation of practitioners from four international accounting firms including their clients, and focused her attention on taxpayers' evaluations of tax services and how these differed from what practitioners offered. Schisler (1995) elicited information from two separate samples, taxpayers and practitioners, and focused on their tax aggressiveness preferences. Stephenson (2007), on the other hand, drew a sample of practitioners and their clients and matched the dyads' views on practitioners' aggressiveness. As some responses could not be matched due to inadequate identification, she carried out two separate analyses, one based on the matched sample and the other on two independent samples. Her results showed there was a gap between views – practitioners were more aggressive than taxpayers thought they were. A wider gap was found in the matched sample than with the independent samples. In all of these studies, investigation was limited to measuring differences in expectations and services, with little attention being paid to understanding how these differences may come about.

As a first step to capturing the dynamic interdependence of taxpayers and tax practitioners, this present research draws on some of the insights provided by the literature discussed above. Taxpayers' primary aims in using a practitioner are to reduce uncertainty and to file a correct tax return. However, clients may also demand, or be curious about, aggressive strategies. As they themselves do not have the 'know-how' to go about it, they have to rely on their practitioners' expertise in devising an appropriate tax strategy for them. Some practitioners, on the other hand, may or may not be willing to give in to the demands of their clients, or they may not feel that they have the capability of responding satisfactorily to their clients' wishes. Others are willing to develop aggressive tax planning strategies knowing that there is a market for them. The effect of practitioners on taxpayer compliance is less clear, but compelling evidence suggests that they are both enforcers and exploiters depending on whether the rules are clear or ambiguous (Blumenthal and Christian 2004:217; Kleppers et al. 1991).

To gain a better understanding of the role of tax practitioners in taxpayers' behaviour, this research examines the role demands and expectations of the client and the role behaviour of both the client and the practitioner. Both views are considered important due to the interactive nature of the transaction between the tax practitioner and the client. The study is grounded in role theory and relies on a social psychological model to provide a theoretical framework for analysing the expectations, perceptions, attitudes, and behaviour of the two parties. In order to provide breadth to the study from both the taxpayers' and tax practitioners' perspectives, an independent sample methodology was used. The questions asked were: How does a sample of taxpayers see and act toward their practitioners? And how does a sample of tax practitioners respond to their clients? The next chapter develops a Tax Practitioner-Client Role Model which is adopted as the framework for this study.

Chapter 3
Conceptual Framework

3.1 Introduction

The literature review discussed in the previous chapter shows that the role of tax practitioners in tax compliance has been considered to a limited extent but that researchers using traditional approaches have not managed to capture the dynamic nature of the working relationship between the practitioner and the client. Furthermore, researchers who conducted studies on practitioners have made no attempt to discuss the concept of 'role.'

According to Parsons (1951:23), a role is,

> that organized sector of an actor's orientation which constitutes and defines his participation in an interactive process. It involves a set of complementary expectations concerning his own actions and those of others with whom he interacts.

Therefore, in considering the role of tax practitioners in tax compliance, the clients' needs and expectations, as well as the practitioners' perceptions of and their response to their clients' expectations must be considered. Certainly, tax practitioners interact with their clients, although the extent of interaction (such as frequency or duration) varies among practitioners and clients.

Drawing on the social psychology literature, this chapter introduces the theory of role dynamics posited by Kahn, Wolfe, Quinn and Snoek (1964). Their model is frequently referred to in studies of role conflict and has been used as a framework for studies in various domains including accounting (see Beck 1974; Cameron 1992; Kleinman and Palmon 2001; Senatra 1976). Based on this model, a preliminary role framework for tax practitioner and client is proposed, and used for the development of hypotheses for this thesis.

3.2 The concept of role

Role theory, according to Turner (2001:233), "deals with the organization of social behaviour at both the individual and the collective levels" and is "a key element in understanding the relationships among the micro-, macro-, and intermediate levels of society." Roles can be viewed as having a corresponding set of expectations and obligations, and they define the appropriate behaviours for a person to perform in the role (Anderson and Kitchener 1998:97). In this functionalist/structural approach to the concept of role it is posited that roles are prescribed by society as a whole, and individuals simply adopt them. This approach is considered to be overly deterministic and static and proponents of it fail to recognise the vast differences in how individuals conceive of their roles. In contrast, the fundamental premise of interactionist social theory is that individuals and groups of individuals interact. Turner (2001:235) posits that individuals,

> shape their own roles so as to interact effectively with the role they attribute to the relevant others. Sometime this is a matter of conforming to expectations, but more fundamentally it is a matter of collaboration, oppositions, or any of many other possible relationships.

Role is therefore more fluid and subtle and the process involves not only role-taking and role-playing but also role-making (Turner 2001).

Prior research that has tapped into role theory tends to ascribe different meanings to the concept of role. Some studies have been focussed on the norms associated with roles, (that is, prescriptive in nature), whilst others have been focussed on beliefs (that is, subjective probability) or preferences (that is, attitudes) (Biddle 1986). As a result, role theory has been criticised for being "vague, nebulous and non-definitive" (Biddle 1986; Morris 1971; Rodham 2000:72).

To clarify the different perspectives used by different role theorists, Biddle (1995) distinguished the concept of role into three types: role as behaviour, role as social position and role as expectation. One does not preclude the others. Role as behaviour refers to behaviours that are characteristic of people who are in similar occupations and professions. Although not everyone in the same occupation or profession will behave identically, there is a pattern of behaviour exhibited by the occupant and they have the potential for affecting, and being affected by, the behaviour of others who interact with them (Biddle 1995; Morris 1971). Role as a social position generally refers to the identity or social position that is shared by those in similar occupations or professions. Role as expectations refers to the expectations held by others of those who are in certain occupations or professions. Some expectations may be widely shared, while others may reflect divergent opinions, and as a result generate role conflicts for the person (Biddle 1995:62).

3.3 Role dynamics

Based primarily on the concept of role as behaviour and role as expectations,[18] and recognising the effects of interaction between individuals, Kahn et al. (1964) developed a more dynamic, contextual framework for understanding the relationships between role expectations and role behaviours within an organisational setting. Their Role Episode Model is used to examine role ambiguity, role conflict, and stress.

As described by Kahn et al. (1964), the role set consists of different people (termed role senders) with whom the focal person has contact. Role senders have a stake in the focal person's performance as they can benefit or be disadvantaged by it. They may also be dependent on the focal person's performance as they may require it to perform their own tasks. Accordingly, they develop beliefs and attitudes about what the focal person should or should not do. The prescriptions and proscriptions held by members of a role set are termed role expectations and they represent the standards for evaluating the performance of the focal person (Kahn et al. 1964). The numerous acts which make up the process of role sending are not merely informational, but are also attempts by senders to influence the focal person to conform to their expectations.

As shown in Figure 3.1, each of the four boxes represents an event that forms a role episode. The expectations/pressures described above are being sent to the focal person and affects the immediate experience of the focal person. This experience typically has

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[18] And, to a lesser extent, role as social position.

both perceptual and cognitive aspects and the focal person's reactions are determined by the nature of his/her experience. Focal persons are also self-senders as they too have a conception of their work and a set of attitudes and beliefs about what they should and should not do while in that position. They have some awareness of what behaviours will fulfil their responsibilities and lead to the accomplishments of their work. Through a long process of socialisation and formal training, they have acquired a set of values and expectations about their own behaviour and abilities. The focal person is thus conceived of as "having an occupational self-identity and is motivated to behave in ways which affirm and enhance the valued attributes of that identity" (Kahn et al. 1964:17).

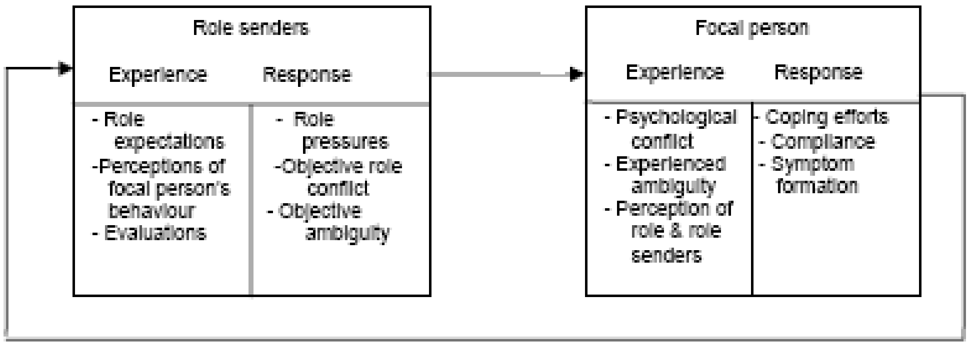

Figure 3.1: Role Episode Model (Kahn et al. 1964:26)

When role pressures are seen as illegitimate or coercive, the focal person may resist the demands of the role sender giving rise to role conflict. Focal persons may respond to role conflict in several ways. For instance, when they find that they cannot realistically conform to an expectation, they may persuade the role senders to modify the incompatible demands (Kahn et al. 1964:29). Alternatively, they may reject or avoid those role senders whose demands they find they cannot meet.

The feedback communicated to role senders may or may not lead to immediate modifications in the demands that role senders make of them. Role conflict, as indicated in the literature on organisational behaviour and theory, cannot be taken too lightly in an organisation as it can lead to disastrous consequences such as work stress or termination of service (Kahn et al. 1964; Schuler 1977a). However, House and Rizzo (1972) argued that the experience of role conflict by the focal persons could be regarded as an indicator that they are performing effectively, particularly people who are occupying high level supervisory roles or boundary-spanning roles in an organisation. In other words, any conflict associated with the coordination of highly differentiated constituencies must be borne in order to achieve successful role performance (Miles 1976:26).

In an organisation, role ambiguity may also arise when there is a discrepancy between the information available to focal persons and that which is required for adequate performance of the focal persons' role. Role ambiguity is generally associated with satisfaction, tension, strain, and anxiety in an organisation context (Miles 1976; Schuler 1977).

In Kahn et al.'s model, the role episode is abstracted from a process which is cyclical and ongoing: the focal person provides feedback to the sender, in a way that either alters or reinforces the demands made of him/her. The next role sending will depend on the sender's evaluation of the response to his/her last feedback and thus a new episode begins.

As indicated by Kahn et al. (1964), the whole process does not occur in isolation; expectations or behaviours are shaped by additional or contextual factors such as organisational characteristics, personality, and the interpersonal relations between the role senders and the focal person.

Organisational characteristics include organisational structure, specialisation, and the formal reward system, and determine in part the role senders' experience, expectations, and the pressures they impose. Personality factors, on the other hand, are those factors which describe a person's propensities to behave in certain ways. They tend to evoke or facilitate certain responses from role senders and shape the focal person's interpretation of the pressures. Also personality dispositions may lead to the use of certain kinds of coping responses. Therefore, they are important determinants of differential reactions to role pressures. Interpersonal relations refer to the more or less stable patterns of interaction between the focal person and the role sender and to their orientations toward each other. They include the power or ability to influence, affective bonds (such as respect and trust), dependence of one on the other, and style of communication. The role perception literature has shown the importance of communication; for instance, the more communication and feedback available to the role sender or focal person, the better s/he is able to cope with role ambiguity and conflict (Schuler 1977b). The kinds of pressures exerted by the role sender upon the focal person therefore depends to some degree upon the nature of relations between them. Pressures will also be interpreted differently depending on the relationship between the focal person and the role sender. Furthermore, any changes in the focal person's feelings and behaviour (for example, loss of trust or respect) are likely to affect their relations, their future role behaviours, and responses to the behaviour.

Although Kahn et al.'s (1964) model is used to examine the dyadic interactions between role senders and focal persons within the same organisation, it can be adapted for studies of other role sets. As the tax practitioner and the taxpayer (the client) are two independent parties (dyads) in a role set, the model could be adapted to provide a suitable theoretical framework for understanding the role of tax practitioners and their clients in a tax setting. The next section explains the development of the Tax Practitioner-Client Role Model.

3.4 Tax Practitioner-Client Role Model

In the context of the provision of tax services, the role set primarily consists of the tax practitioner, the taxpayers, the government, the practitioner's affiliated professional bodies and society. However, since this study sets out to provide an understanding of the tax practitioner-client relationship and their roles in tax compliance, the role set is focused on the tax practitioner who is presented as the focal person and the taxpayer who is presented as the role sender.

Drawing on the tax compliance literature and Kahn et al.'s (1964) role model, a conceptual framework of the role of the practitioner and client in a tax setting was developed and is shown in Figure 3.2. It is based on their perceptions of each other and indicates that each one's decisions or actions can be influenced by his/her characteristics, and environmental and interpersonal relationship factors. The development of this framework involves two stages. First, the application of the role concept to how taxpayers and their practitioners interact needs to be articulated. Once the notion of a taxpayer-tax practitioner episode is accepted, the question arises of patterning of role performance and responsiveness across episodes. For taxpayers, there are repeated exposures to tax practitioners; sometimes one practitioner, that contributes to this patterned manifestation of role expectation and performance. For tax practitioners, patterning in the roles they adopt comes about through repeated exposures to different clients. It is this transituational model of role expectation and performance that is the subject of this thesis.

The first stage in adapting Kahn et al.'s work was to consider what a snapshot of each encounter (or episode) that takes place between the practitioner and the client might look like. Each encounter involves a sequence of activities that takes place as follows: expectations (or activities that s/he requires the practitioner to perform) are sent from the client to the practitioner; these are perceived and evaluated by the practitioner in relation to the expectations of the client, which then leads to responses by the practitioner.

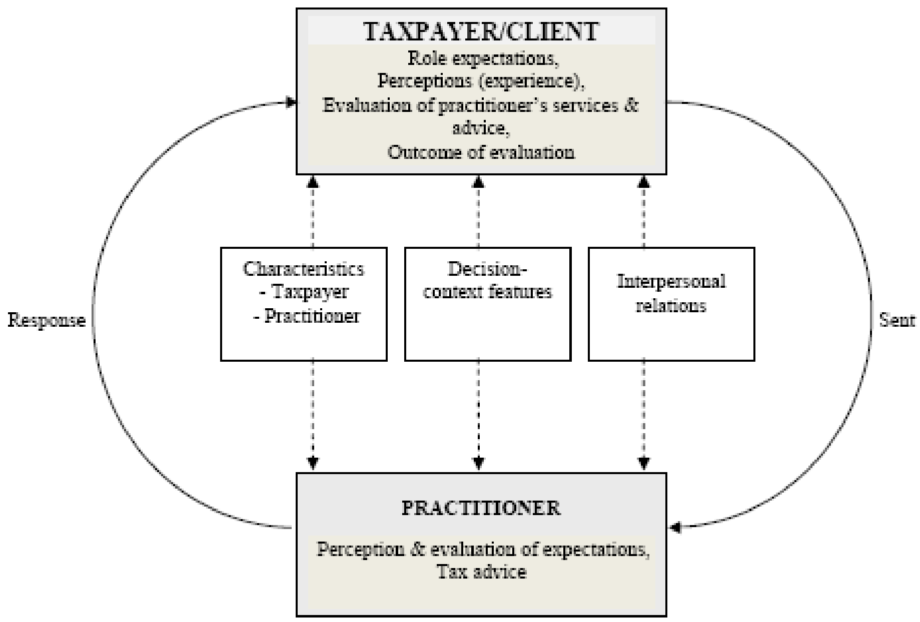

Figure 3.2: Tax Practitioner-Client Role Model in a tax setting and factors affecting their role

The client observes and evaluates the practitioner's response in relation to his/her expectations and needs, and reacts to the practitioner's response. Taxpayers who find that practitioners are not conforming to their expectations may accept the practitioner's response or may put pressure on him/her to conform. The whole process of sending and responding is cyclical and ongoing and the number of encounters depends on the number and complexity of the tax issues involved - the more complex the issue, the more likely the number of encounters will increase.

Over time, taxpayers and practitioners settle into their preferred modes of engagement. While some elements will be peculiar to a particular interaction between a taxpayer and his/her practitioner, other elements of the role will generalise across encounters. Taxpayers become aware of their own expectations and can articulate how they perceive their practitioner. It is possible to ask, 'What are the messages sent to practitioners by taxpayers?' and 'How do these messages vary by person, context and relationship?' Similarly, the question can be asked, 'How do practitioners interpret the messages of their clients?' and 'How do these perceptions differ by person, context and with the perceived characteristics of the role sender?'

A number of outcomes of role messages sent and received, and of roles performed are important in this analysis. An outcome from a client's evaluation of a practitioner's services is satisfaction or dissatisfaction with the fulfilment of role expectations. Another is the willingness of the client to either retain or terminate the practitioner's services in the future and to accept or reject advice.

Among the most important outcomes for practitioners are role conflict, role ambiguity, and advice given. Practitioners may encounter problems with their roles, especially when they are subject to incompatible role expectations (role conflict) where, for instance, they are required to provide advice in accordance with their clients' conflicting demands. A good example is where clients expect their practitioners to help them file a safe tax return as well as to help them exploit tax loopholes. What some clients demand of their practitioners can also be inconsistent with the practitioners' ethics or moral values (Biddle 1979). These types of demands place the practitioners in an awkward situation; they want to establish good relations with clients so as to maintain the client base but the goals and values of their clients do not match their professional integrity.

If role conflict exists, then practitioners must have ways to resolve it. For example, they could comply with clients' demands, as otherwise they may lose clients. Or they may persuade clients to modify the incompatible demands so as not to breach professional values and conduct. Practitioners may also reject some clients' demands, if they believed economic harm would result for either or both of them. Such a reaction means that they are willing to terminate their relationship, especially with those who want to evade tax. Another approach that practitioners may use is to communicate effectively with their client and engage in solving the problem jointly (Kahn et al. 1964). Therefore, depending on the practitioners, their coping response could take a number of forms: from succumbing, to adapting to clients' demands, to solving problems jointly, to terminating the client relationship.

Apart from role conflict, practitioners may experience role ambiguity which arises when the demands or expectations of taxpayers are not explicitly communicated (Kahn et al. 1964). Practitioners who misread what their clients really want may inadvertently provide advice that is contrary to their clients' preferences. Therefore, there could be a mismatch between the expectations perceived by both parties giving rise to role ambiguity. As pointed out in Ssection 2.4.4, a possible consequence of role ambiguity is that practitioners may provide aggressive (or conservative) advice to conservative (or aggressive) clients thinking that they wanted this type of advice. Another potential consequence of miscommunication is that it may affect clients' evaluation of practitioners' services, as practitioners act in accordance with their perceptions of clients' expectations (Christensen 1992; Hite et al. 2003; Spilker, Worsham and Prawitt 1999).

In the Tax Practitioner-Client Role Model it is recognised that the two parties' expectations and behaviours are dynamic. They are a function of the interaction of different characteristics, different motives, and values, different sensitivities and fears, different habits and the like (Kahn et al. 1964). As practitioner and client interact over time, mutual learning and understanding takes place, which can help ease the initial conflicts they have. As these conflicts give way to increased mutual understanding, the outcomes of their interactions tend to be influenced by other factors such as the decision maker characteristics and behavioural norms (Kleinman and Palmon 2000).

This framework is in accord with the tax literature which indicates that the characteristics of the client and tax practitioner, their interpersonal relations and extrinsic or situational factors or what Milliron (1988) categorised as decision context features, influence tax decisions. Personal characteristics and interpersonal relations essentially reflect psychological and social development, whereas decision context features arise outside the dyads in the taxpaying environment.

Based on the Tax Practitioner-Client Role Model discussed above, this study drew on two perspectives, that of business taxpayers and that of tax practitioners. From the business taxpayers' perspective, this study examined their expectations and perceptions of practitioners' services and their tax reporting decisions. From the tax practitioners' perspective, their perceptions of role expectations and practice, role conflict, role ambiguity, and tax reporting decisions will be examined. The study further investigated the effects of the following factors on practitioners' and clients' tax decisions where the tax law is ambiguous: characteristics of practitioners and clients, features of decision context, and the interpersonal relationship between practitioners and clients. The potential effects of these factors are examined in the following chapter in which a set of research hypotheses are developed.

3.5 Chapter summary

The Role Episode Model developed by Kahn et al. (1964) providess a suitable theoretical framework for research on the roles of tax practitioners and their clients in tax compliance as it recognises the relevance of the interactions between parties within a role set. Prior studies which considered considered factors that may influence taxpayers' or tax practitioners' tax decision making researchers failed to take into account such interactions. Tax practitioners interact with their clients, although there may be variations in frequency, duration, medium, and diversity of contacts.

Adapting this framework, the Tax Practitioner-Client Role Model was developed. The model is focused on the two independent parties, the service provider (the tax practitioner) and the client (the taxpayer). The role process consists of a set of demands made by taxpayers on their practitioners. On the basis of their perceptions of the clients' demands, practitioners have their own views of what demands they should try to meet, given their type of social position. In keeping with Kahn et al.'s theoretical formulation, in the framework the characteristics of taxpayers and of tax practitioners, their interpersonal relations, and features of decision context that may have an impact on their decision making are all taken into consideration. The concept of practitioner-client role in this thesis is considered in terms of an umbrella concept covering (a) the demands placed on practitioners by clients and their evaluation of practitioners' response, (b) practitioners' perception of clients' demands and their response, and (c) the drivers of practitioners' and taxpayers' behaviour.

A major implication of this role model is that the perceptions and behaviours of the tax practitioners need to be measured independently of the perceptions and behaviours of the taxpayers. The research strategy adopted in this study therefore involves observing the role expectations, role performance, and behaviours as reported by a sample of taxpayers and a sample of tax practitioners. Each of the taxpayers in the sample would serve as the data source for him/herself as well as being the informant about the behaviour of his or her practitioner. Similarly, each of the practitioners in the sample would provide an account of his/her role, and as well as being the informant about the role demands and behaviour of his or her clients. These observations will help us to make better sense of the taxpayers' motives and goals in engaging a practitioner and their willingness to accept their practitioners' advice. It will also help us to gain further insights into how practitioners see their own role and the challenges they face.

The next chapter discusses the factors that affect their decision making in more detail and develop research hypotheses for testing.

Chapter 4
Research Hypotheses

4.1 Introduction

In Chapter 3, a Tax Practitioner-Client Role framework was developed to serve as a guide for hypothesis development. The formulation of the research hypotheses to represent the taxpayers' and tax practitioners' perspectives are discussed in Part I and Part II respectively. The hypotheses are specified at the outset and subsequently justified. In this chapter, it is important to note that business taxpayers are playing a role in response to their conceptualisation of their tax practitioner and practitioners are playing a role in response to their conceptualisation of their clients.

Part I: Expectations and responses of business taxpayers

4.2 Hypotheses representing the business taxpayers' perspective

From the business taxpayers' perspective, this study focused on two main aspects of their role relationships with their tax practitioners. In the first set of hypotheses taxpayers' expectations, experiences, evaluation, and commitment to their practitioners were examined by testing the following hypotheses:

> H1 (taxpayers): There will be an expectation/experience gap between taxpayers' expectations and experiences with the services provided by practitioners.

> H2 (taxpayers): The expectation-experience gap will have a negative effect on satisfaction with, and intention to retain, practitioners' services.

> H3 (taxpayers): Taxpayers' trust in practitioners will have a positive effect on satisfaction and intention to retain practitioners' services.

Expectations represent the messages that taxpayers send to their tax practitioners, that is, their own focal persons. Experience represents the responses from these persons. Trust represents the role senders' generalised understanding of the kind of relationship they have with the focal person that extends across time and context. These three hypotheses are summarised in the research model in Figure 4.1 below:

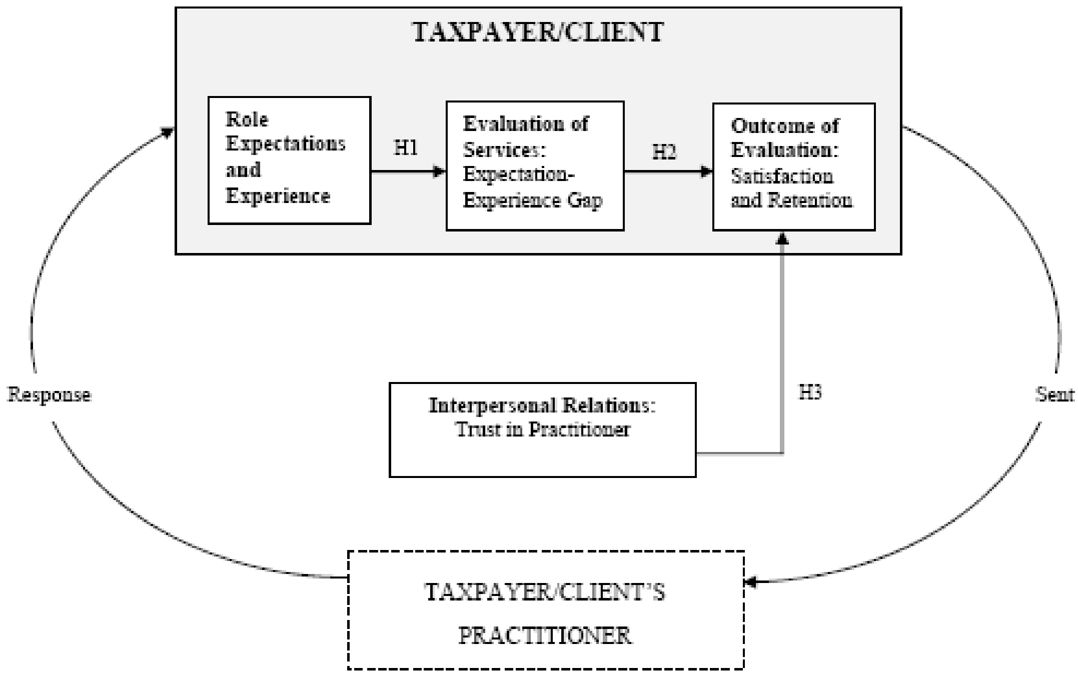

Figure 4.1: Representing Hypotheses 1, 2 and 3 (taxpayers) within the Tax Practitioner-Client Role Model

The second set of hypotheses examined whether variations in taxpayers' tax reporting decisions when their practitioners provided aggressive advice was explained by their expectations of aggressive advice, personal tax ethics, business tax ethics, risk propensity and sanction risk perceptions. The hypotheses that were tested are as follows:

> H4 (taxpayers): In an ambiguous tax situation, expectations of aggressive advice will be positively associated with taxpayers' agreement with practitioners' aggressive advice.

H5 (taxpayers): In an ambiguous tax situation, personal tax ethics will influence taxpayers' agreement with practitioners' aggressive advice.

H6 (taxpayers): In an ambiguous tax situation, perceived business tax ethics will influence taxpayers' agreement with practitioners' aggressive advice.

H7 (taxpayers): Taxpayers with a higher risk propensity will agree more with their practitioners' aggressive advice on an ambiguous tax situation than will those with a lower risk propensity.

H8 (taxpayers): Taxpayers with low sanction risk perceptions (perceived probability of detection and of severe tax penalties) will agree more with their practitioners' aggressive advice on an ambiguous tax situation than will those with high sanction risk perceptions.

These five hypotheses are summarised in the research model in Figure 4.2 below:

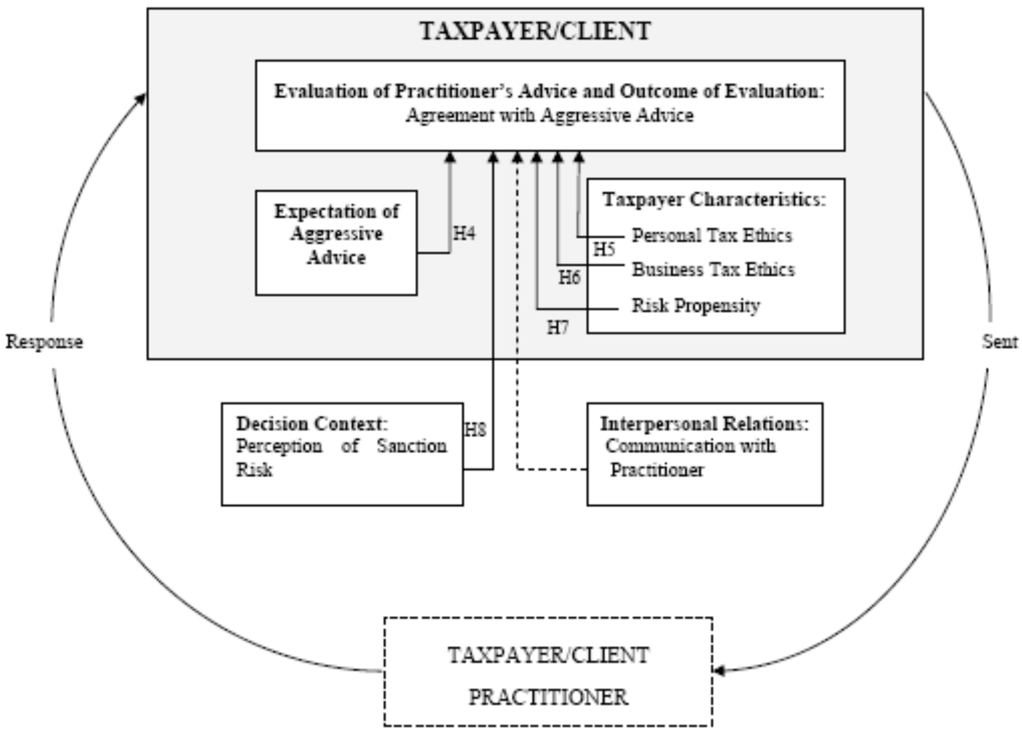

Figure 4.2: Representing Hypotheses 4, 5, 6, 7 and 8 (taxpayers) within the Tax Practitioner-Client Role Model

The potential impact of the interpersonal relation factor on taxpayers' agreement with aggressive advice is represented in a dotted line, as it was not tested quantitatively due to its interactive nature. Instead, it was teased out from the qualitative data.

In the remainder of Part 1 of this chapter, these eight hypotheses are discussed in the context of the available literature.

4.2.1 Expectation and experience, evaluation and outcome

The Tax Practitioner-Client Role framework discussed in Chapter 3 shows taxpayers as role senders with certain expectations of their tax service providers. Expectations could be formed by taxpayers, for instance, based on their needs, their past experiences with a tax practitioner, or interpretation from the advertisements placed by tax practitioners about what they can do for their clients. Taxpayers' expectations are pertinent in a practitioner–client role relationship as they represent the basis for action, that is, they energise efforts to trigger a desired behaviour or to thwart an undesirable behaviour by the tax practitioner (Kleinman and Palmon 2001:101). They will vary with taxation beliefs, past experiences and perceptions of practitioner role norms. However, not all taxpayers share similar expectations. For instance, taxpayers may expect their practitioners to help them with any or all of the following activities: saving tax, minimising tax, reducing audit risk, resolving uncertainties, paying the correct amount of tax, avoiding serious penalties, and exploiting tax loopholes (Collins et al. 1990; Dubin et al. 1992; Smith and Kinsey 1987; Klepper et al. 1991; Long and Caudill 1987; Scotchmer 1989; Yankelovich, Shelley and White Inc. 1984).

In the practitioner-client tax setting modelled in Figure 4.1, once expectations are sent to practitioners, the practitioners' responses are fed back. The taxpayers then perceive these responses and evaluate them against their expectations. The first question then is, 'Do taxpayers perceive themselves receiving from the practitioner the services they expected?' Or, specifically, 'Is there an expectation-experience gap, that is, expectation is greater than what is experienced?' Christensen's (1992) results showed that taxpayers felt that they did not receive as much tax planning assistance as they expected from their practitioners. Change and Bird's (1993) study revealed a significant gap between what clients expected to save from tax by using an adviser and what clients felt their adviser actually helped them save.

Support for the expectation gap hypothesis emerges from other studies (such as those conducted by Duncan et al. 1989; Hite et al. 1992; Murphy and Byng 2001; Pei et al. 1992). Taxpayers have been found to be more risk averse than their practitioners overall (Hite et al. 1992; Tan 1999) - which may be why they rely on practitioners for help to minimise their taxes legitimately. There are also practitioners who gave more conservative advice even to clients who expected aggressive advice (Duncan et al. 1989; Pei et al. 1992). The mounting evidence in the marketing literature further supports the mismatch between clients' expectations and service providers' performance. Service providers, in general, may not always understand what consumers expect from their service (Parasuraman, Zeithaml and Berry 1985) because expectations are not clearly communicated to practitioners, or taxpayers themselves have conflicting expectations (Sakurai and Braithwaite 2003). Even if practitioners understand what clients expect of them, they may not be willing to meet clients' demands because they conflict with their professionalism. Overall, these studies suggest that taxpayers' expectations may not always be congruent with their experiences of practitioners' service. Therefore, the first research hypothesis for taxpayers posits that:

> H1 (taxpayers): There will be an expectation/experience gap between the taxpayers' expectations and experiences with the services provided by practitioners.

What is even more interesting is what happens when taxpayers' expectations are not met. There are two possible outcomes. The taxpayers could resort to putting more pressure on the practitioner to comply with their requirements. Should this fail, then the outcome may be dissatisfaction with the service and as a consequence termination of the practitioner as a tax service provider. But this may not necessarily be the case. As shown in the studies by Tan (1999) and Murphy (2001), the intention of clients to retain or dismiss their practitioners was not influenced by the type of advice provided by the practitioners even if it was contrary to their preferred advice. It appears that other factors may have an impact on the outcomes of their evaluations, but there is not much empirical research that explores the effects of the expectation-experience gap further. Christensen's study (1992) on tax services merely indicated that clients were satisfied when their expectations for tax service quality were met or exceeded. Chang and Bird's (1993) study suggested that clients experienced an expectation gap but they did not examine the repercussions of the gap. Further, it is possible that even though taxpayers expect practitioners to meet their needs and demands, they are also open to influence from their practitioners (Sakurai and Braithwaite 2003). Ascertaining these outcomes would provide useful insights into the working relationship between the practitioner and the client.

Research in the marketing domain has indicated that there is a direct link between customer satisfaction (and service quality) and future retention (or commitment/loyalty) of service provider, and that satisfaction with services is related to confirmation or disconfirmation of expectations (Brown and Swartz 1989; Fullerton and Taylor 2002; Garbarino and Johnson 1999; McDougall and Levesque 2000; Smith and Houston 1982; Tosi 1966). Overall satisfaction (or cumulative satisfaction) is defined as "an overall evaluation based on the total purchase and consumption experience with a good or service over time" (Anderson, Fornell and Lehmann 1994:54; Jonas and Frey 2003). These findings suggest that a customer's evaluation is not based on only one particular type of advice or recommendation. Rather, it is based on his/her summated experiences with the service provider. Tan (1999) and Murphy (2001) used only a hypothetical scenario to gauge whether or not taxpayers would retain their practitioner. Consequently, the survey instrument may not have captured other expectations of clients which may be considered equally important in their decision to retain or switch practitioners.

These interesting insights into the practitioner-client relationship raised the following research questions: what happens when taxpayers find that their expectations are not met, that is, when there is an expectation/experience gap? Will such a gap influence satisfaction with services and future retention of practitioner? To test these research questions, the following hypothesis was developed:

> H2 (taxpayers): The expectation-experience gap will have a negative effect on satisfaction with, and intention to retain, practitioners' services.

Apart from the possible influence of an expectation-experience gap on client satisfaction and retention of practitioner, the interpersonal relations between the two parties are also considered an essential ingredient for a successful relationship and continuity of a relationship (Garbarino and Johnson 1999). One important dimension of interpersonal relations that is singled out in the social psychology literature is trust (Kahn et al. 1964).

As pointed out by Sniezek and Van Swol (2001:289), one who depends on another for advice inevitably confronts "social uncertainty", that is, an inability to predict perfectly whether or not the advisor is giving the best possible advice. In the context of tax advice, taxpayers solicit the advice of tax practitioners who are the tax experts to help them solve their tax problems. However, even with a detailed explanation of the advice from a tax practitioner, the taxpayer in most instances may still have insufficient understanding to eliminate all uncertainty about what is best. However, when the client trusts the practitioner, social uncertainty is reduced. Trust in contexts of information asymmetry of this kind is described by Scholz (1998) as the "trust heuristic". The client relies on the trust heuristic to move forward in the belief that the practitioner is acting in the client's best interests.

Trusting the practitioner is therefore an important factor in a relationship as it signifies that taxpayers confidently believe that the tax practitioner is not only competent but can be relied upon to behave in such a manner that the long-term interests of the taxpayer will be served (Barber 1983; Braithwaite and Levi 1998; Crosby, Evans and Cowles 1990:70; Sniezek and Van Swol 2001).

Taxpayers also tend to be more open and cooperative if they trust their advisers (Boccaccini, Boothby and Brodsky 2004). Trustworthiness is more broadly associated with having greater capacity to influence and change the way in which individuals behave (Makkai and Braithwaite 1993). Trust in the practitioner may therefore cause taxpayers to modify or compromise their expectations to bring them in line with what practitioners have to offer. Since clients' trust in their practitioners could play a critical role in their working relationship, it is hypothesised that even if there are differences in opinion, trust is associated with satisfaction and retention of practitioners as follows:

> H3 (taxpayers): Taxpayers' trust in the practitioner will have a positive effect on satisfaction with, and intention to retain, practitioners' services.

4.2.2 Evaluation of practitioners' aggressive advice and outcome

One of the reasons why taxpayers engage the service of tax practitioners is to help them to arrive at a satisfactory tax position where the tax law is uncertain. As the literature suggests, tax practitioners contribute to compliance by enforcing legally clear requirements stipulated in the tax law (Klepper and Nagin 1989a). However in ambiguous situations, different practitioners appeared to resolve the issue in different ways (Carnes et al. 1996b), with some being more aggressive than others. With many aspects of the tax law not clear cut, there are indeed ample opportunities for practitioners to exploit them to their clients' advantage. Aggressive advice provided by practitioners is therefore of particular concern to the tax authorities. Hence, an interesting research question here is, 'Will taxpayers subscribe to the practitioners' aggressive advice where the tax law is unclear, or will their decisions be driven by other factors?'

Figure 4.2 shows a part of the Tax Practitioner-Client Role Model that focused specifically on this particular aspect of their role relationships, that is, their agreement with aggressive tax advice provided by their practitioners.

Taxpayers may seek the advice of practitioners, but in the eyes of the law, they (and not the practitioners) bear the full responsibility of paying the correct amount of tax. Accordingly, when practitioners provide feedback on their recommendations, taxpayers as shown in the Tax Practitioner-Client Role Model in Figure 4.2 will have to make a tax reporting decision. That is, they have to evaluate and respond to the practitioners' recommendation. The outcome of such an evaluation is to agree or disagree with the aggressive advice and in the model several factors that could potentially influence the taxpayers' decision are posited. The factors considered in this study are: (a) expectation of aggressive advice, (b) personal tax ethics, (c) business tax ethics, (d) personal risk propensity, and (e) sanction risk perceptions. The influences of these factors are examined as the literature indicates that these economic and social psychological factors are important contributors toward taxpaying behaviour. Five hypotheses were developed and are discussed below.

Since the Role Model is interactive in nature, their manner of communication must also play an important role in the practitioners' decision making (see dotted line in Figure 4.2). Because of variability in communication methods and the relatively unexplained nature of this aspect of practitioner-client interaction, interpersonal relations are explored qualitatively from the data elicited from the open-ended questions.

Taxpayers' expectation of aggressive advice

From a role perspective, taxpayers have expectations of their practitioners which are discussed in Section 4.2.1. An expectation is "an anticipation of future consequences" (Grover and Vriens 2006:576), and the content of these expectations may include preferences with respect to specific acts (Kahn et al. 1964:14). Studies have shown that taxpayers' preference for type of advice might influence their agreement with their practitioners' advice and the literature indicates that taxpayers' preference for type of advice varies. Some taxpayers prefer conservative advice while others prefer aggressive advice (see for example, Hite and McGill 1992; Leung and Cooper 2005; Sandford and Dean 1972; Tan 1999). However, in some studies no attempt has been made to examine whether or not taxpayers' preferences are dependent on the ambiguity of tax law. The literature which indicates that taxpayers' preference is to be on the safe side of the law (see for example, Sakurai and Braithwaite 2003) suggests that if the tax law is clear, taxpayers would prefer conservative advice; whereas if the tax law is ambiguous, they might prefer aggressive advice.

Therefore, drawing from the findings on taxpayers' preference for type of advice, together with practitioners' responses to tax law ambiguity, it was hypothesised that those who expect aggressive advice, where the tax law is ambiguous, will be more likely to agree with practitioners' recommended aggressive advice. The fourth hypothesis is stated as follows:

> H4 (taxpayers): In an ambiguous tax situation, expectations of aggressive advice will be positively associated with taxpayers' agreement with practitioners' aggressive advice.

Taxpayers' personal and business tax ethics

As a person's behavioural intentions to comply or not comply with tax law are posited to depend on the norm (Ajzen 1991; Fishbein and Ajzen 1975), this factor has received considerable attention in tax research (Kirchler 2007; Reckers, Sanders and Roark 1994; Torgler and Murphy 2004; Wallschutzky 1984; Wenzel 2002). Personal norms or tax ethics refer to "privately held ethical and moral convictions" (Wenzel 2005a:213) and have been identified as an important determinant of taxpaying behaviour (Alm, Sanchez and De Juan 1995; Wenzel 2005a). Studies have also shown that taxpayer ethics play a mediating role between compliance variables such as opportunity, probability of detection (Smith, 1990; Wenzel 2002), tax rate, taxpayer's withholding status (Reckers et al. 1994), and probability and severity of consequences (Wenzel 2002).

A social norm represents "a pattern of behavior that is judged in a similar way by others and that is sustained in part by social approval or disapproval" (Alm et al. 1995:6). As pointed out by Spicer and Lundstedt (1976), human behaviour in the area of taxation can be affected by internalised norms of role expectations and these norms may be affected by the behaviour of an individual's reference groups (such as friends, relatives, work associates etc.). Consequently, if taxpayers know that many people in groups important to them evade taxes, then their commitment to the social norm of tax compliance will be weaker (Alm et al. 1999). Although some studies have shown that social norms indeed play a role in shaping taxpayers' behaviour (Alm et al. 1995; Wenzel 2005b), their relevance appears less clear, at least compared to the effects of personal norms on tax compliance (Kirchler 2007; Wenzel 2005a). For instance, taxpayers who view tax evasion as immoral (personal norms) may not necessarily evade tax even if others do (social norms). The explanation for this behaviour offered by Wenzel (2005b) is that social norms can be effective only when taxpayers identify with the group to whom the norms are attributed. This reasoning perhaps explains why some taxpayers are affected by social norms (Vogel 1974) while others adhere to their own tax ethics (Braithwaite 2000; Grasmick and Bursick 1990; Reckers et al. 1994; Sheffrin and Triest 1992).

The literature on the effect of taxpayers' personal and social norms on taxpayers' compliance behaviour suggests that these norms could also play a part in business taxpayers' reporting decisions. That is, the extent to which business taxpayers are willing to accept aggressive advice from practitioners could be influenced by their own personal norms (termed here as personal tax ethics). In addition, they could also be influenced by their perceptions of other businesses' social norms (termed here as business tax ethics). Accordingly, the following hypotheses posit that:

> H5 (taxpayers): In an ambiguous tax situation, personal tax ethics will influence taxpayers' agreement with practitioners' aggressive advice.

> H6 (taxpayers): In an ambiguous tax situation, perceived business tax ethics will influence taxpayers' agreement with practitioners' aggressive advice.

Taxpayers' risk propensity

As the tax treatment of certain income and expenses is not always clear cut, taxpayers who are confronted with such uncertainties will have to make a choice as to whether or not to accept their practitioner's advice. Decisions they make could be characterised as risky when they are faced with high uncertainty "about whether potentially significant and/or disappointing outcomes of decisions will be realised" (Sitkin and Pablo 1992:10). The decision making behaviour literature identified risk propensity as having an impact on decision makers' behaviour (Sitkin and Pablo 1992; Sitkin and Weingart 1995). Risk propensity refers to an individual's tendency, on average, to take or avoid risks. While there is some evidence that willingness to take risks is situationally determined (see for example, prospect theory), risk propensity is also seen as a personality trait. The psychological and criminological literature shows that there are people with high and people with low risk propensity (Sitkin and Pablo 1992). Compared to those with a propensity to avoid risks (risk averters), those who are willing to take risks (risk takers or risk seekers) are more likely to construe a relatively risky situation as one of low risk, and thus have a higher tendency to take risks (Wong 2005).

The decision makers considered in this study are business taxpayers. As entrepreneurs they would have experienced different types of risks. That said, individual differences in willingness to take risks are still likely to exist. For instance, some taxpayers may claim an expense only when they are very certain that the expense is deductible. This group may be considered as taxpayers with low risk propensity, that is, they are risk averters. On the other hand, there may be taxpayers who do not require a very high level of certainty that an expense is deductible. They may think that they have a plausible story for why it should be and they will give it a go and see if it is accepted. This group of taxpayers have the characteristics of risk takers. Risk propensity is therefore a relevant factor that could affect willingness to accept practitioners' aggressive advice. In Tan's (1999) study, which showed that taxpayers accepted whatever advice their practitioners gave, she did not consider the possible impact of individual taxpayers' risk propensity. Several studies suggest that risk propensity varies among taxpayers (Chang et al. 1987; Collins et al. 1990; Hite and McGill 1992; Sakurai and Braithwaite 2003). Accordingly, it was hypothesised that when practitioners offer aggressive advice, it is likely that those business taxpayers who are risk takers will be more willing to accept aggressive advice than will those who are risk averters. The hypothesis is stated as:

> H7 (taxpayers): Taxpayers with a higher risk propensity will agree more with their practitioners' aggressive advice on an ambiguous tax situation than will those with a lower risk propensity.

Taxpayers' sanction risk perception

The effects of audit probability as compared to severity of penalty have consistently been shown to affect taxpaying behaviour (see for example, De Juan, Lasheras and Mayo 1994; Friedland 1982; Kinsey and Grasmick 1993; Klepper and Nagin 1989a; Mason and Calvin 1978; Schwartz and Orleans 1967; Webley and Halstead 1986). These results support the economic model, in which the assumption is that taxpayers are self-interested, and generally engage in tax evasion if it pays (Kirchler 2007). Studies have indicated that the probability of detection is the most significant factor to affect tax positions adopted on contentious tax issues, and tax evasion (Kaplan et al. 1988; Modeo et al. 1987; Webley et al. 1991). However, many researchers have argued that it is the perceived likelihood of detection rather than the actual probability of detection that has an impact on compliance behaviour (Braithwaite et al. 2001; Christensen and Hite 1997; Jackson and Milliron 1986; Mason and Calvin 1978). Taxpayers' compliance is likely to be higher when they perceive a high probability of being caught and suffering severe consequences (De Juan et al. 1994; Friedland, Maital and Rutenberg 1978; Grasmick and Bursik 1990; Klepper and Nagin 1989; Lewis 1982; Richardson and Sawyer 2001; Schwartz and Orleans 1967).

These views are in accord with the perceptual deterrence literature, which has shown that people differ in how likely they think it is that negative sanctions will impact on them in both economic and social domains (Nagin 2000; Zaleskiewicz 2001:106). Risk perception refers to a decision maker's assessment of the risk inherent in a situation, that is, how risky a situation is in terms of probability estimates of the degree of situational uncertainty (Sitkin and Weingart 1995:1575). Those who perceive a situation to be high risk tend to be more risk averse and those who perceive a situation to be low risk tend to be more risk seeking.

Drawing from both these literatures, taxpayers who are faced with a decision as to whether to agree or disagree with their practitioners' aggressive advice when the tax law is ambiguous may also be influenced by their own assessment of sanction risk, that is, the certainty and severity of punishment (Nagin 2000). This effect would operate above and beyond the overall risk-taking propensity discussed in the previous section. It is a situational measure of risk taking when an ambiguous tax issue is involved (Christensen and Hite 1997). The following research hypothesis tests the effects of sanction risk perceptions as follows:

> H8 (taxpayers): Taxpayers with low sanction risk perceptions (perceived probability of detection and of severe tax penalties) will agree more with their practitioners' aggressive advice on an ambiguous tax situation than will those with high sanction risk perceptions.

4.2.3 Control Variables

Taxpayers' firm size

One factor that has a marked influence on the taxpaying of business taxpayers is firm size. In particular, small businesses have been identified as major contributors to the US income tax gap (Hite et al. 1992; Slemrod 2004). To some extent, such findings imply that small businesses are more aggressive than large corporations, but other studies call into question this inference. This aggressive characteristic of small businesses in some ways appears inconsistent with results from studies indicating that a small business organisation's (SBOs) most important aim is to file an accurate tax return (Collins et al. 1990; Hite et al. 1992; Tomasic and Pentony 1991). Other researchers (for example, McBarnet 2003) adopt the view that creative compliance is more pervasive in large corporate practice. Tax practitioners also indicated that, compared to small clients, large clients expected them to be more aggressive (Tomasic and Pentony 1991). Possibly, evasion is the method of reducing tax that is more commonly identified in small businesses, especially those involved in the cash economy (Morse, Karlinsky and Bankman 2009). Large businesses are more likely to use avoidance measures effectively to reduce their tax.

Apart from these inconsistent findings, there are very few research studies focusing on the effect of firm size on agreement with practitioners' advice. Tan's (1999) sample consisted of mainly small businesses[19] and her results suggested that small businesses tended to have a preference for conservative rather than aggressive advice. Hite et al.'s (1992) findings showed that a huge majority of SBOs were risk averse as they would claim a deduction only if they were 70% certain that it would be allowed. Although this study points towards the conservativeness of small firms, no comparisons could be made with large firms as they were not included in their sample. It is interesting that a recent study by Ahmed and Braithwaite (2005) showed that small businesses preferred a tax practitioner who is creative and knowledgeable about aggressive tax planning, and they admitted greater tax evasion than those employed in the nonprofit sector.

Taking into consideration the literature on the potential relation between size of business and decision making, firm's size was used as a control variable in this study.

Taxpayers' audit experience

It has been further suggested in the literature on decision making that decision makers' experience or familiarity with a situation can have an impact on their subsequent behaviour (Kirchler 2007). In a tax context, it is possible that taxpayers' audit experiences may have an effect on their tax decisions. However, taxpayers who have been audited before could experience either a negative (sanctions imposed) or positive (no sanctions imposed) outcome. As Tittle (1980) suggested, the type of outcome experienced before could affect future tax compliance behaviour. A positive (or negative) audit experience may encourage (or discourage) future tax compliance. For instance, strategic tax evaders exposed to tax audits may learn to develop more effective noncompliance strategies (Erard 1992). As a result, they might be more willing to undertake risks that

[19] Her sample consisted of 80% of firms with a turnover of less than $2 million and 90% of the firms employed fewer than 50 employees.

less experienced individuals would usually avoid. Other researchers have argued that taxpayers who have been audited before might not necessarily react in this manner (Andreoni et al. 1998). It is possible that taxpayers whose audits failed to detect noncompliance may conclude that they may not be so lucky next time (Klepper and Nagin 1989a:131). Drawing on this literature, those who are deciding on whether or not to accept their practitioner's aggressive advice may also reflect on their audit experience. Since the results appeared mixed, audit experience was also used as a control variable in this study.

Part II: Expectations and responses of practitioners

4.3 Hypotheses representing the tax practitioners' perspective

From the tax practitioners' perspective, this study was focused on two main aspects of their role relationships with taxpayers. The Tax Practitioner-Client Role framework demonstrates that the actions of practitioners are a product of messages sent by the client and interpreted and acted upon by the practitioner in the context of his/her own beliefs and practices. In this thesis, two aspects of the practitioners' world are of interest: (a) role conflict and how it is managed and (b) the giving of aggressive as opposed to conservative advice to clients on ambiguous tax decisions.

Following the format of the previous sections on taxpayers, the practitioners' hypotheses are first summarised and illustrated diagrammatically and then discussed individually as relevant literature is reviewed. First, the tax practitioners' perspective is examined in relation to role conflict tested through the following hypothesis:

> H1 (practitioners): Practitioners experience role conflict as there will be gaps between their perceptions of what their clients expect of them and what they actually do for their clients in practice.

This hypothesis is summarised in the research model in Figure 4.3 below

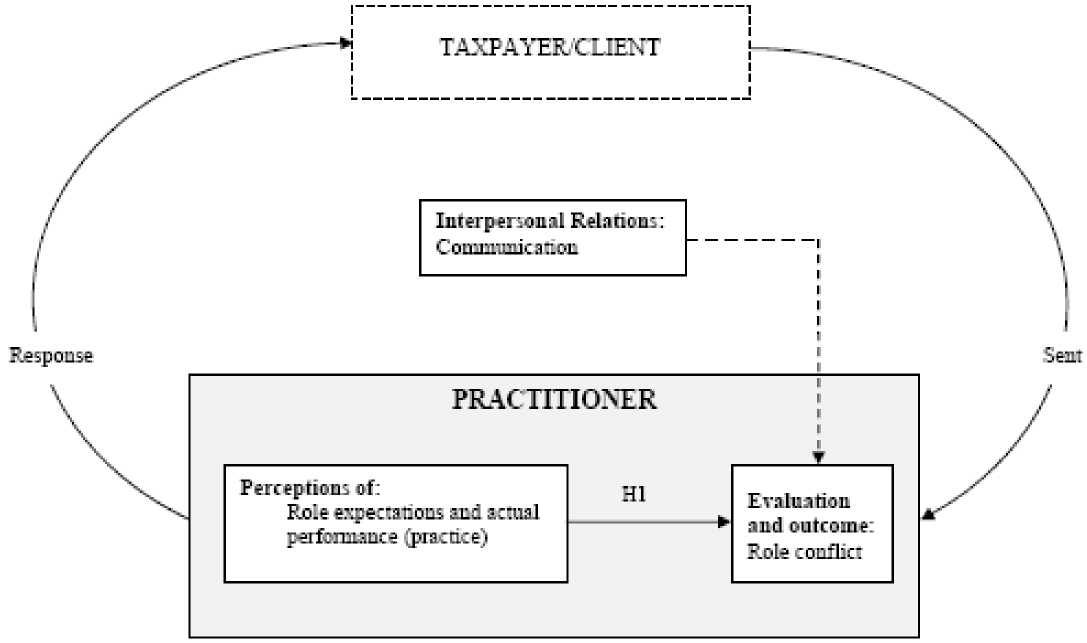

Figure 4.3: Representing Hypothesis 1 (practitioners) within the Tax Practitioner-Client Role Model

An interesting question raised in this thesis is, 'If practitioners experience role conflict, how do they cope with it?' The model postulates that their interpersonal relations, particularly their way of communicating with clients, may mediate role conflict. Because of variability in communication methods and because this is relatively unexplored territory, data were not collected on this issue through closed-ended questions. Instead, this study drew on the responses provided by the practitioners from the open-ended questions and explored the relationship between this aspect of interpersonal relations and role conflict qualitatively (see dotted line in Figure 4.3).

The second aspect of the practitioners' role relationships was focused on the type of advice given in ambiguous tax situations. A set of hypotheses were developed in which variation in tax practitioners' tax advice is explained by variation in practitioners' perceptions of clients and their own personal characteristics. The perceived client characteristics considered important were personal risk propensity, and the clients' sanction risk given the decision context. The practitioners' characteristics considered important were practitioners' ethics and practitioners' risk propensity. The hypotheses that were tested are as follows:

> H2 (practitioners): Practitioners' perceptions of clients' risk propensity (aggressive or conservative) will have an effect on their recommended advice in an ambiguous tax situation, with aggressive advice being given to clients who are perceived as risk taking and conservative advice being given to clients perceived as risk averse.
>
> H3 (practitioners): Practitioners' perceptions of clients' sanction risk (audit probabilities and severity of tax penalties) will have an effect on their recommended advice in an ambiguous tax situation, with aggressive advice being given if they perceived low sanction risk and conservative advice given if they perceived high sanction risk.
>
> H4 (practitioners): Practitioners' personal tax ethics will have an effect on the type of advice (aggressive or conservative) recommended by them to clients in an ambiguous tax setting, with those who compromise their ethics offering more aggressive advice.
>
> H5 (practitioners): Practitioners' risk propensity will have an effect on the advice recommended by them to clients in an ambiguous tax setting, with aggressive advice being given by those with a higher risk propensity and conservative advice being given by those with a lower risk propensity.

Since interpersonal relations are an important aspect of the practitioner-client relationship as suggested in the Role Model (see dotted line), the manner of communication with each other may influence their decision making. For the same reasons mentioned earlier, that is, due to its interactive nature, their manner of communication cannot be examined directly, but must be teased out from the qualitative data obtained from the open-ended questions.

These four hypotheses are summarised in the research model in Figure 4.4 below:

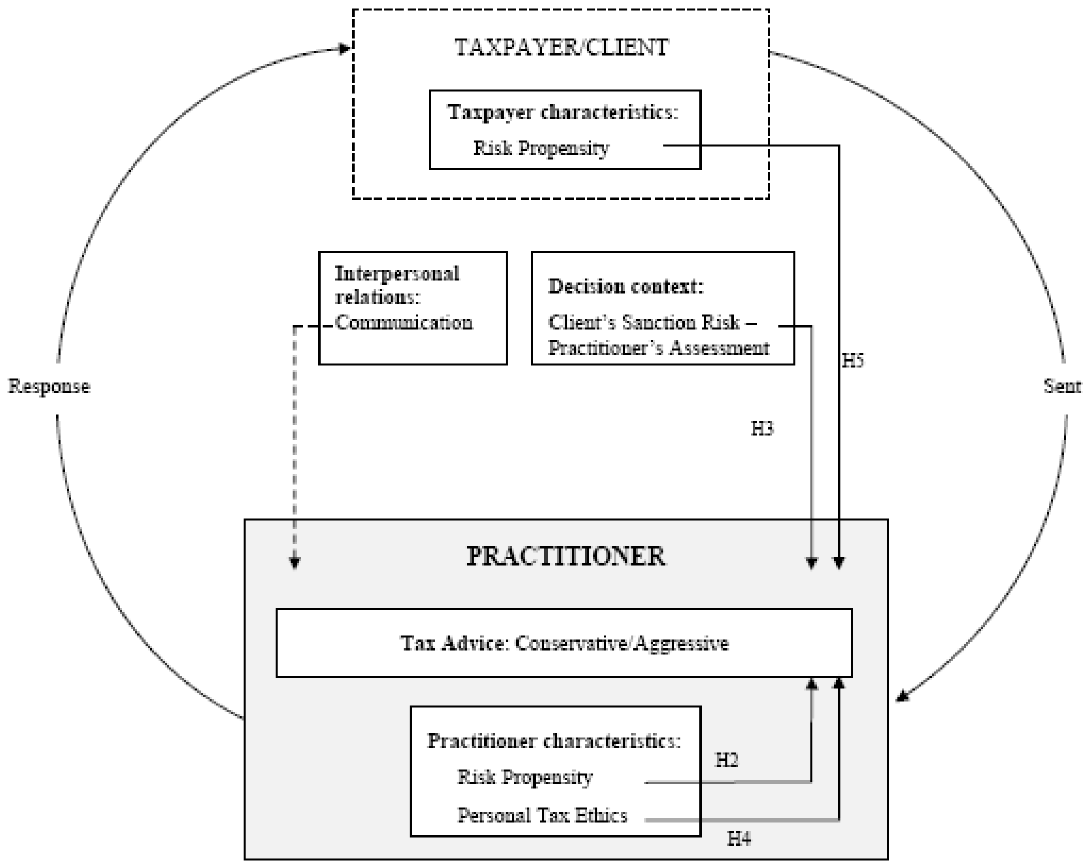

Figure 4.4: Representing Hypotheses 2, 3, 4 and 5 (practitioners) within the Tax Practitioner-Client Role Model

4.3.1 Expectation-practice gap - role conflict

In the practitioner-client tax setting modelled in Figure 4.3, expectations sent by clients are perceived and evaluated by the practitioner. Central to the Tax Practitioner-Client Role Model is the notion that practitioners can be subject to incompatible role expectations (role conflict) and possibly miscommunication (role ambiguity).

Taxpayers, as discussed in Section 4.2.1, have several expectations or demands of practitioners. However, some of the role expectations may not be compatible with others. For instance, taxpayers may expect practitioners to help their firm avoid tax penalties. At the same time they may expect practitioners to provide them with aggressive advice to minimise tax. Sakurai and Braithwaite's (2003) study provides some evidence of the conflicting needs of taxpayers. This type of role conflict is termed intra-sender conflict, that is, where different prescripts from a single member of the role set are incompatible (Kahn et al. 1964).

Another type of conflict, person-role conflict may be experienced by the practitioner when expectations of others and personal expectations fail to coincide. As tax service providers, practitioners are expected to deliver their service in accordance with their clients' expectations. However, practitioners' perceptions of clients' expectations may not always coincide with what they practise as they have their own perceptions of what their role entails. They have to consider their legal responsibilities and their professional code of ethics, in the case of those affiliated with a professional body, when recommending a tax position for their clients. If taxpayers' demands are overly aggressive, practitioners may not be willing to meet those demands, as they may be illegitimate or violate their professional integrity.

Therefore, practitioners may be aware of clients' expectations but may consider them to be overly demanding or outside the letter of the law. Practitioners are faced with role conflict if, on the one hand, they do not want to succumb to taxpayers' demands, but on the other, they want to maintain a good relationship with their clients. They try to fulfil the role of client advocate while adhering to the demands of other constituencies such as the IRD and the accounting profession (Yetmar and Eastman 2000). Such situations would not be uncommon in a tax setting, as the literature indicates. Therefore, it is hypothesised that there will be inconsistencies between what their clients expect of them and what they do in practice.

> H1 (practitioners): Practitioners experience role conflict as there will be gaps between their perceptions of what their clients expect of them and what they actually do for their clients in practice.

When tax practitioners experience role conflict, it invokes a feeling of internal emotional distress that they will attempt to resolve or reduce (Grover 1993:254). There are a number of ways in which practitioners could cope with role conflicts. For instance, they may view some of their clients' expectations as overly demanding or outside the legal boundaries of the tax law and attempt to convince their clients to change their expectations. On the other hand, some may accommodate their clients' expectations by changing their own expectations of their role. Another conflicting resolution is to terminate their working relationship. How role conflict unfolds can be influenced by interpersonal dimensions such as communication (Kahn et al. 1964). In this study, insights into how communication might influence outcome were teased out from tax practitioners' responses to open-ended questions.

4.3.2 Practitioners' tax advice and its influences

As shown in the Role Model, clients seek the advice of tax practitioners when they are unsure of the appropriate treatment of an income or expense. When the tax law is ambiguous, tax practitioners help their clients to resolve the issue in hand. As tax service providers and client advocates, practitioners would most likely resolve ambiguous tax issues in their clients' favour. However, as the compliance literature suggests, there are a number of practitioner-specific factors that could influence practitioners' decisions or recommendations when faced with ambiguous tax issues (Carnes et al. 1996a; Kaplan et al. 1988; Roberts 1998). Figure 4.4 shows these factors in a partial Tax Practitioner-Client Role Model: perception of clients' risk propensity, and practitioners' own assessments of clients' sanction risk, tax ethics and risk propensity.

The following hypotheses were developed to test whether any of these factors explain the variation in practitioner tax reporting decisions/recommendations in an ambiguous tax setting.

Perceptions of clients' risk propensity

Studies performed on tax practitioners suggest that they view their clients as the initiators of aggressive tax reporting (Attwell and Sawyer 2001; Klepper and Nagin 1989a; Schisler 1994; Tooley 1992). However, in these studies there was no examination of whether or not practitioners comply with such requests. In other studies the effects of client factors on tax practitioners' reporting decisions or recommendations have been examined. In some studies (for example, Duncan et al. 1989; Helluloid 1989, Pei et al. 1992), tax preparers' decisions were found not to be influenced by clients' attitudes toward risk. Others (for example Cloyd 1995; Cuccia et al. 1995; Milliron 1988; Schisler 1994) showed that client aggressiveness influenced practitioners' advice.

The implication of these findings is that if clients expect aggressive (or conservative) advice, practitioners provide that type of advice (LaRue and Reckers 1989). Perhaps such a strategy is used by practitioners to manage the risk propensity of their clients. Practitioners are well aware that they could easily lose a dissatisfied client to other tax service providers if they do not respond in accordance with their clients' wishes.

That said, it is unlikely that they will yield to clients who demand aggressive advice if the tax law is clear cut. To do so will only make their clients unnecessarily vulnerable to tax penalties and cause themselves to be seen as irresponsible. But where the tax law is ambiguous, they may use their professional judgement to exploit tax loopholes to satisfy clients' wishes. After all, aggressive advice is not tax evasion, and some clients are willing to take risks. Since the literature suggests that practitioners may act in empathy with taxpayers and tailor their advice to suit their clients (LaRue and Reckers 1989, Roberts 1998; Schisler 1994), the following hypothesis was tested:

> H2 (practitioners): Practitioners' perceptions of clients' risk propensity (aggressive or conservative) will have an effect on their recommended advice in an ambiguous tax situation, with aggressive advice being given to clients who are perceived as risk taking and conservative advice being given to clients perceived as risk averse.

Tax practitioners' assessment of clients' sanction risk

Two types of decision context features relate to clients' sanction risk, that is, probability of audit and severity of tax penalties (Carnes et al. 1996a; Milliron 1988). Both have the potential to affect tax practitioners' tax reporting decisions where the tax law is ambiguous. However, the effects of sanction threats on tax practitioners have produced mixed results (see, for example, Duncan 1989; Kaplan et al. 1988; LaRue and Reckers 1989; Newberry et al. 1993). For instance, in the study conducted by Madeo et al. (1987) on tax practitioners' reactions to experimentally manipulated income levels, tax rate progressivity, size of penalty and likelihood of detection suggest that the probability of detection exerts the strongest influence. Kaplan et al. (1988) reported that experimentally manipulated probability of audit (of 50%) significantly influenced the type of advice rendered by professional tax practitioners. LaRue and Reckers (1989), however, found that the perceived likelihood of an IRS audit (of 10% and 25%) had no effect on CPAs' willingness to encourage aggressive reporting for a real estate tax shelter. The inconsistent results could be due to the way the audit probability and severity of penalty were operationalised. For example, some probability of audit rates used in these studies were weaker (such as 5%, 10% or 25% chance of audit) than others (40% or 50% chance of audit). As such, the differently rated probability of IRS audit makes it difficult to compare their results and draw inferences for hypothesis generation. In addition, the penalty examined in these studies is the preparers' penalty in the US and there is no such penalty in New Zealand. In this sense, practitioners in these studies are reporting on the risks to themselves (since they can be penalised under US law).

In contrast, this study was focused on practitioners' perceptions of sanction risks to their clients. As discussed earlier for taxpayers' sanction risk in Section 4.2, it is argued that perceptions of sanction risk are more influential on aggressive decisions than the actual risks. This perceptual approach is also well supported by researchers in deterrence (Simpson 2002). As noted by Paternoster (1987:174), "deterrence was most likely to depend on what the certainty and severity of punishment were thought to be rather than on their objective or actual levels."

Practitioners with their experience in tax work may have their own perceptions of the probability that their clients would be audited and would face severe penalties. On this basis, when faced with a grey area or an ambiguous decision, practitioners may respond in an economically rational manner, that is, they may weigh the perceived costs and benefits of recommending an aggressive tax position (Roberts 1998). Even though it is their clients and not they themselves who may be audited and penalised, they are likely to feel that the occurrence of such sanctions may damage the client-practitioner relationship (Marshall et al. 2006). Practitioners' perceived likelihood of audit and penalties could therefore have an impact on the type of advice they provide to clients. Accordingly, the hypothesis is stated as follows:

> H3 (practitioners): Practitioners' perceptions of clients' sanction risk (audit probabilities and severity of tax penalties) will have an effect on their recommended advice in an ambiguous tax situation, with aggressive advice being given if they perceive low sanction risk and conservative advice being given if they perceive high sanction risk.

Practitioners' personal tax ethics

As Kahn et al. (1964:17) posit, each practitioner has some awareness of what behaviours will fulfil their responsibilities and lead to goal accomplishment. Practitioners have a set of attitudes and beliefs about what they should, and should not, do in their role. Through a long process of socialisation and formal training, practitioners would have acquired a set of values and expectations about their own behaviour and abilities.

The link between personal ethics and decision making is not immune from pressure. Duty to the client may be perceived to conflict with personal values as may duty to the government or duty to their professional body's ethical guidelines. As a client's expectations or preference for advice moves along the continuum from conservative to aggressive to clearly fraudulent, it is not always obvious at which point the practitioner should abandon advocacy and insist on less aggressive reporting. The fear of losing clients to competitors will intensify their personal moral dilemma (Pilkington 1998). As indicated by Cruz et al. (2000), client pressure for aggressive reporting creates a complex professional judgment involving both technical and ethical considerations. The increasing importance of retaining the client may cause tax practitioners to put their values to one side and to adopt those of the client, or take other action to neutralize their own ethical behaviour (Yetmar, Cooper and Frank 1998:9).

Practitioners who are affiliated to an institution such as the NZICA, NZLS, or TINZ have to comply with the stipulated code of ethics of these organisations. Nevertheless, it is often difficult to judge if the standards have been met due to the uncertainties surrounding many tax issues. For instance, practitioners who are members of the NZICA have to adhere to their code of ethics which stipulates that:

> "A member performing tax work is entitled to put forward the best position in favour of a client, or an employer, provided the work is performed with competence, does not in any way impair integrity and objectivity, and is in the opinion of the member, consistent with the law. The member may resolve doubt in favour of the client or the employer if in the member's opinion there is reasonable support for the position" (Para 49).

What constitutes "reasonable support" is not defined and appears to be left to the individual practitioner's professional judgement. The findings of Tooley's study (1992) and Attwell and Sawyer's study (2001) which indicated that the majority of practitioners had encountered ethical problems in discharging their responsibilities raised concerns about the level of ethics shown by tax practitioners.

Ethics can be viewed in a hierarchical pyramid according to Schweikart (1992:475). If a practitioner uses legally binding rules or statutes (externally defined) as a yardstick, then his/her ethics are at the lowest level. The next step up the ethics pyramid is where practitioners' decisions are made within a professional code of conduct and are not necessarily based on following a rule book. The highest level of ethics is displayed when practitioners' decisions are made within a highly defined narrative of right and wrong developed through moral and philosophical reasoning. For taxation, this could mean that legal rules are interpreted not necessarily literally, but rather through the spirit of those rules. However, practitioners in carrying out their role have different perceptions of behaviour that are considered moral or ethical (Karcher 1996). Therefore, practitioners' personal tax ethics could influence their aggressiveness in terms of tax advice to clients. Song and Yarbrough (1978) provided empirical evidence to support the mediating role of ethics on behaviour. Their study showed that attitudinal factors, which encompassed the moral beliefs of tax practitioners, influenced their professional conduct. Since tax practitioners' personal ethics have the potential to influence their tax advice, the following research hypothesis was tested:

> H4 (practitioners): Practitioners' personal tax ethics will have an effect on the type of advice (aggressive or conservative) recommended by them to clients in an ambiguous tax setting, with those who compromise their ethics offering more aggressive advice.

Practitioners' risk propensity

Tax practitioners' risk propensity is a potential determinant of the type of advice they will offer to their clients. The literature on risk propensity has been discussed in Section 4.2.2 and will not be repeated here. Tax practitioners who resolve ambiguous tax issues in their clients' favour certainly take more risks as there is the possibility that the tax position may not be upheld by the tax authority or the courts. Although earlier studies (for example, Milliron 1988) suggest that risk attitudes only weakly influence aggressiveness, later studies indicate significant effects. These studies showed that tax professionals' advice was markedly more aggressive when the professionals indicated that they were willing to accept more risk with respect to decisions made for their clients (Carnes et al. 1996b; Pei et al. 1990).

Since there is substantial evidence that shows risk propensity has some influence on practitioners' judgements or recommendations, the research hypothesis was set out as follows:

> H5 (practitioners): Practitioners' risk propensity will have an effect on the advice recommended by them to clients in an ambiguous tax setting, with aggressive advice being given by those with a higher risk propensity and conservative advice being given by those with a lower risk propensity.

4.3.3 Control variables

Practitioners' firm size

Prior researchers have investigated the effects of various socio-demographics on tax reporting decisions by practitioners. One of the characteristics examined is the size of their firms, and the findings suggest that this may have an influence on the role they play in taxpaying behaviour. Bigger firms, as compared to smaller firms, are generally perceived to be more likely to comply with their clients' aggressive requests (see for example, Kinsey 1999; Tomasic and Pentony 1991). Perhaps bigger firms have more resources to support their practitioners, making them more experienced in dealing with tax law ambiguity than practitioners from smaller firms.

Research results show that within the professional class of CPAs in the US, significant differences in reporting recommendations are found between those employed by large versus small firms (Carnes et al. 1996b; Helleloid 1989; Sanders and Wyndelts 1989). Other findings show that there are attitudinal differences between CPAs employed by different sized firms (Cuccia 1995). Those working for the (then) Big 6 firms were more aggressive for high ambiguity scenarios (Carnes et al. 1996b) when compared to non-Big 6 firms. Ayres et al. (1989) reported no difference in professionals' judgements across firm type (that is, the (then) Big 8 versus non-Big 8). Perhaps the mixed results reflect differences in competitiveness in different contexts. It might be argued that smaller practitioner firms may feel greater pressure from clients and ignore ethical standards in contexts of high competition for clients' business (Coyne and Smith 1987; Roth et al. 1989). Based on these mixed research results, firm size was used as a control variable in this study.

Practitioners' firm identification

Although practitioners act as individuals, they also act as members of groups. The identities gained from membership of professional groups can be particularly influential in affecting behaviour (Biddle 1979). Some studies (Ayres et al. 1989; Carnes et al. 1996a; Cuccia 1994; Erard 1993; McGill 1988) suggest that those who are affiliated with a professional body such as CPAs are more aggressive or more pro-taxpayer than non-CPAs in their interpretation of the law (primarily in the deduction cases). However, other studies generally have revealed weak or no effect of CPA membership on aggressiveness (for example, Ayres et al. 1989; Cuccia 1994; Duncan et al. 1989; Schisler 1994; Stephenson 2007). A recent study by Hite and Hasseldine (2003) showed that CPA-prepared returns resulted in fewer audit adjustments for deduction items, but not for income items, than non-CPA returns, suggesting that CPAs are not consistently more aggressive as suggested in prior research.

The New Zealand studies are particularly interesting in relation to professional group membership because anyone can practise as a tax practitioner in New Zealand. Thus, practitioners may be affiliated with the NZICA (New Zealand Institute of Chartered Accountants), the TINZ (TaxAgents Institute of New Zealand Incorporated), the NZLS New Zealand Law Society), each having its own code of ethics, or may not belong to any professional bodies. Studies in which the influence of professional membership on advice has been examined have produced mixed results. Tooley's (1992) study, for instance, showed both accountants and lawyers as being considerably less disapproving of avoidance measures than were other tax agents, but no significant differences were found between the groups in aggressive tax decisions/recommendations. In contrast, Attwell and Sawyer (2001) showed that tax agents, as compared to lawyers and Chartered Accountants, were the group that least disapproved of tax avoidance. Despite lack of clarity in findings, membership of a professional organisation, that is, firm identification could be a potentially important factor shaping the giving of aggressive advice, and therefore it was used as a control variable in this study.

Practitioners' tax experience

The literature has indicated the potential impact of experience on tax practitioner judgements (Duncan et al. 1989; Jackson et al. 1988; Kaplan et al. 1988, Reckers et al. 1991). Carnes et al. (1996a) argued that more experienced professionals have better-developed knowledge structures, and may be more conservative as they look beyond client factors such as importance. Instead, their advice is based on the facts and circumstances of each case (Gibbins 1984). Where tax law is ambiguous, studies have shown that increased aggressiveness is positively related to experience levels. For instance, Hite and McGill's (1992) study showed that more experienced tax professionals from the (then) Big 8 accounting firms tended to be more aggressive. Similarly, more experienced tax managers of the (then) Big 6 firms were found to show greater tax minimisation tendencies than were less experienced managers in Pei et al.'s (1992) study.

Other studies have shown little, or no, relation between the number of years of experience and aggressiveness (Ayres et al. 1989; Cuccia 1994; Duncan et al. 1989). The inconsistent findings could be due to the varying ranges of practitioners' experience adopted in those studies (see for example, Carnes et al. 1996a).

It could be argued that practitioners who have had more years of experience would have encountered a greater diversity of tax situations, including ambiguous situations. They would also have had more experience in obtaining feedback and judging the legitimacy of their recommendations. However, it could also be that experienced practitioners from smaller firms have been involved in routine and straightforward tax services and despite their years have not been involved in more sophisticated tax problems. For these reasons, it is possible that experience would have no impact. Due to these different possibilities, experience is introduced as a control variable.

4.4 Chapter summary

The literature reviewed in Chapter 2 provided insights into the role played by tax practitioners in taxpaying behaviour. However, the lack of a conceptual framework makes it difficult to generalise predictions or explain the roles played by the taxpayer and tax practitioner in tax compliance. This chapter draws on the Tax Practitioner-Client Role Model developed in Chapter 3 and formulated several research hypotheses to test the model.

Taxpayers generally have some idea of the role that tax practitioners should play when they engage their services. The Tax Practitioner-Client Role Model posits that taxpayers have certain expectations of their tax practitioners and that when their experience with practitioners' services falls short of expectations, it will give rise to an expectation-experience gap. It was hypothesised that there would be an expectation-experience gap as taxpayers' general perception is that practitioners can do much more to save tax or provide tax planning advice (Chang and Bird 1993; Christensen 1992). Such a gap can also arise when clients' expectations are not clearly communicated to practitioners or when taxpayers themselves have conflicting expectations (Sakurai and Braithwaite 2003).

When evaluating the services provided by practitioners, it was hypothesised that taxpayers with the proposed expectation-experience gap would feel dissatisfied with practitioners' services. Consequently, taxpayers may terminate the services of the practitioner. This thesis asserted that a gap would be negatively related to satisfaction and retention of practitioners. However, if taxpayers and practitioners had built up good interpersonal relationships, this may alter taxpayers' evaluations of their practitioners' services. The interpersonal relations variable considered important in this study is taxpayers' trust in their practitioners, that is, the more taxpayers trust their practitioners, the more likely they are to feel satisfied with their practitioners' services, and the more likely they are to retain their services. This means that the practitioner-taxpayer relationship is not necessarily destabilised by the gap alone.

As the Tax Practitioner-Client Role Model shows, client expectations are perceived and evaluated by practitioners. They have perceptions of what their clients expect of them, some of which they may share, while others may violate the practitioners' beliefs and values and their professional integrity. For these reasons, it was hypothesised that practitioners would experience role conflict. How practitioners cope with role conflict is an interesting area to explore and their qualitative feedback provided some insights into coping responses that can be explored more systematically in the future.

The second way in which this study advances current understanding of how practitioners and taxpayers influence each other is through examining the factors that predict the giving and taking of aggressive advice. Taxpayers seek practitioners' advice to help them resolve uncertainties, and practitioners are known to exploit tax loopholes to the taxpayers' advantage. If practitioners provide aggressive advice, will taxpayers agree with them? What influences their decision? The literature suggests that it depends on the expectations or preferences of taxpayers, that is, whether they prefer aggressive or conservative advice (Hite and McGill 1992; Tan 1999). The Tax Practitioner-Client Role Model posits that apart from taxpayers' expectations, the characteristics of the individual taxpayer (personal tax ethics, business tax ethics, and risk propensity) and features of the decision (sanction risk perception in relation to audit probability and penalty severity) all have a role to play in taxpayer decision making.

Drawn from the literature on taxpayer compliance is the fact that taxpayers' ethics have the potential to influence their tax decisions, that is, their approval or disapproval of aggressive advice could depend on their tax ethics. Furthermore, their decisions concerning aggressive advice could also be affected by their perception of the ethics of other businesses. If taxpayers believe that other businesses are aggressive in tax matters, then they may also adopt aggressive postures. Furthermore, those who are in business may be more prepared to take risks although the level of risks they are willing to take may differ. Therefore, the risk propensity of business taxpayers is likely to have an impact on their tax reporting decisions. It was hypothesised that those with higher risk propensity would be more willing to accept aggressive advice from their practitioners than would those with lower risk propensity. Apart from these characteristics, taxpayers are likely to consider the chance of being audited and the severity of the penalty should their tax reporting decisions be challenged by the tax authority. If they perceived the likelihood of sanction risk as high, it is hypothesised that they may be less likely to accept aggressive advice. As there is potential for firm size and audit experience to impact on taxpayers' decisions, these variables are used as control variables.

What about the tax practitioners? Will they offer aggressive advice to all clients or are their decisions driven by other factors? The literature suggests that when tax law is ambiguous practitioners help their clients to exploit tax law. The Tax Practitioner-Client Role Model posits that practitioners' perceptions of clients' risk propensity, practitioners' own assessments of clients' sanction risk and practitioners' tax ethics and personal risk propensity all have the potential to influence practitioners' recommendations.

Perceptions of a client's risk propensity is an important factor in practitioner recommendations because practitioners are well aware that they could lose dissatisfied clients to other tax service providers if they do not respond in accordance with their clients' wishes. Therefore, it is likely that practitioners will provide the type of recommendation in accordance with their perceptions of each individual client's risk propensity. It could be a strategy that they use to manage clients' varying levels of risk propensity. It was also hypothesised that clients' audit and penalty risk would have an effect on practitioners' recommendations. Before they advise on tax positions for their clients, practitioners may weigh the perceived costs and benefits of recommending an aggressive tax position: that is, they may consider the audit and penalty risk that their clients may face if the tax position is challenged. Their perception of the likelihood of these risks, therefore, could impact on their tax recommendations.

Also important are the practitioners' ethics, that is, their approval or disapproval of aggressive advice may rest on commitments to the spirit of the law, not just the letter of the law. The role of practitioners is complex because on the one hand they have a duty to serve the interests of their clients, but on the other they have a duty to the government and their affiliated professional body. These different demands may pose ethical conflicts for tax practitioners. Clients who pressure for aggressive reporting call upon practitioners to make a complex professional judgement involving both technical and ethical considerations. The fear of losing clients to competitors will intensify their personal moral dilemma and some may compromise their own ethics by offering more aggressive advice. Practitioners' ethics therefore may have a substantial part to play where tax law is uncertain. Also making its presence felt in such situations is practitioners' propensity for risk taking. In addition, there is potential for practitioners' firm size, professional affiliation, and tax experience to impact on decisions. These three variables, therefore, are used as control variables.

The next two chapters focus on understanding the process of dealing with advice from the taxpayers' perspective. Chapter 5 discusses the collection of data from taxpayers and the measurement of concepts. Chapter 6 provides a discussion of the results from testing the set of taxpayer hypotheses. Data collection from tax practitioners and the results of hypotheses testing from the practitioners' perspective are presented in Chapters 7 and 8 respectively.

Chapter 5
Data Collection From Business Taxpayers

5.1 Introduction

The previous chapter developed the research hypotheses and highlighted the theoretical concepts that might affect how taxpayers and tax practitioners engage with the process of tax advising. This chapter describes the method used to gather data from the business taxpayers. The data collection from tax practitioners is discussed in Chapter 7. Descriptive statistics and the initial psychometric analyses are presented in this chapter so as to provide some background information about the respondents and the measures. More detailed analysis for the purpose of testing the hypotheses is discussed in Chapter 6.

This chapter is organised in the following manner. First, the method of data collection is explained. This is followed by a description of the respondents' profile and background. Then, a discussion of how the conceptual model was operationalised is recorded, detailing and evaluating measures in readiness for hypothesis testing in the next chapter.

5.2 Data collection

There are various ways to collect data and each method has its own advantages and disadvantages. In this study, essential questions involved the relative importance of various aspects of role definition and conflict resolution in explaining how tax practitioners and taxpayers came to support aggressive tax planning. This meant that a large sample (over 100) was required for hypothesis testing with multiple regression analysis. The most economical way of obtaining such a sample was through a mail or telephone survey. A self-administered mail questionnaire was selected for reasons of cost and convenience for respondents. Face-to-face interviewing would probably have been more expensive for the researcher and telephone interviewing would have been difficult given that business taxpayers and practitioners are likely to be busy people who are difficult to contact. Even so, respondents would need to set aside time to think about the questions that were posed to them and business owners and tax practitioners would have been unlikely to have been able to have devoted time and effort if they had been asked to respond over the telephone. The use of a mail survey meant that they could choose a time that fitted in with the other demands on their time. Second, a mail survey can capture a broad range of explanatory variables such as taxpayers' perceptions, beliefs and attitudes, and expectations.

Like any method of data collection, mail questionnaires have disadvantages. Poor response rates are one of them and the concern over this drawback is that it may result in nonresponse bias (Kerlinger 1986). Poor quality response is another concern as respondents may either misinterpret or misunderstand the questionnaire, or attempt to conceal their behaviour by responding in a socially desirable manner (Collins et al. 1990; Roth et al. 1989). For this study, various precautions as suggested by Oppenheim (1992)[20] were taken to minimise the potential adverse effects of using self-administered questionnaires.

Closed-ended questions are usually used in self-administered questionnaires, as they are more specific, suited to comparisons, and easy to code and analyse. Generally, closed-ended questions attract higher response rates than open-ended questions as the latter consume more of the participants' time and effort. However, closed-ended questions have limitations. They have been criticised for limiting respondents' answers to the survey, as their predetermined answers may not cover all possible responses. Neuman and Kreuger (2003) point out that something important may be lost when an individual's beliefs and feelings are forced into a few fixed categories. As a result of these limitations, in this study closed-ended questions were supplemented with some open-ended questions.

Open-ended questions produce qualitative data and allow respondents the most opportunity to explain their answers and reactions to the question. Accordingly, data collected in this manner provide more detail and are richer in description. They are also most useful when it is not possible to compile a comprehensive list of options for

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[20] Some of Oppenheim's (1992:104-105) suggestions include an explanation of sample selection, sponsorship of the study, assurance of confidentiality of information, anonymity, and sending of reminders.

respondents. Feedback received from open-ended questions can be used to supplement or substantiate findings from the quantitative analysis and provide a platform for developing quantitative measures for future research.

For this study, a structured questionnaire was developed with approval granted from the Australian National University (ANU) Human Research Ethics Committee. The questionnaire for taxpayers consisted of 105 questions set out in an 11 page booklet. A mixture of open-ended and closed-ended questions was used. Measures of the central concepts are discussed in Section 5.7 below. Data on demographic characteristics and other background information were also collected and are described in Section 5.6.

The questionnaire was initially pilot tested[21] and on this basis, changes were made to improve it. As this study was focused only on taxpayers who engaged the services of a tax practitioner, a filter question was used at the beginning of the questionnaire to identify those who did not use a tax practitioner. Those who indicated that they used a practitioner were asked to complete the questionnaire. Those who did not use a practitioner were asked to return the questionnaire using the reply paid envelope and were given the option of disclosing their firm's name so that a reminder would not be sent.

Copies of the questionnaire and the covering letter are provided in Appendix B.

5.3 Sample

The New Zealand Yellow Pages™ with contact details of businesses in New Zealand was used as the sampling frame. A random sample of 1,400 business taxpayers' addresses was obtained from the Yellow Pages business search service. It was expected that most businesses would provide their contact information there. Although it would have been

21 The pilot sample considered questionnaires for both taxpayers and practitioners. The practitioners consisted of a team of experts from one of the Big 4 accounting firms, another tax expert from the NZICA who was previously the National Tax Director of another Big 4 accounting firm, and one regional tax practitioner. The PhD students were from the Centre for Tax System Integrity, Australian National University. Two small regional business taxpayers also assisted with the pilot test.

ideal to have selected a random sample to represent different sized businesses that is, small, medium and large, the business search database did not have this facility. Since a huge majority (96%) of businesses in New Zealand are small and medium enterprises (SMEs), it was expected that the majority of respondents would represent SMEs. To ensure that there would be some representation from large enterprises, another 100 companies were randomly selected from the New Zealand Exchange Market (NZX). The total number of companies listed on the NZX at the time the sample was drawn was 221.

The questionnaire was addressed to the managers or business owners of the firm. For the listed companies, it was addressed to the Chief Financial Controller. A cover letter (see Appendix B) explaining the purpose of the survey and a reply-paid envelope were enclosed. The letter assured participants that their responses were confidential and anonymous and that only summarised results would be reported. One reminder, containing a further copy of the questionnaire was sent three weeks after the first mailing.

The original intention in the study was to supplement the data obtained from the self-administered questionnaire by interviewing both dyad members, that is, the business taxpayer and his/her practitioner. This would have provided the richest kind of qualitative data on how the taxpayer-practitioner role relationship was negotiated. Accordingly, respondents were asked whether they would be willing to be interviewed along with their practitioners. A separate card was enclosed to elicit their response to the request and to provide contact details if they were agreeable. However, since none of the respondents wanted to disclose their tax practitioners' contact details,[22] no interviews were carried out on the dyads as had been originally planned. The design of the study therefore involved a sample of business taxpayers and an independently drawn sample of tax practitioners described in Chapter 7.

[22] Some respondents indicated that they have no time for interviews.

5.4 Response rates

Of the 1,500 questionnaires sent out, 262 respondents returned completed questionnaires.[23] About 204 of the questionnaires sent out to businesses were identified as out of frame Those that were out of frame were either no longer in business, not known at the address, or did not use a practitioner. This gave an effective sample size of 1,296, with a response rate of 20%.

The response rate, although not high, is comparable to many other tax surveys carried out in Australia and New Zealand. As indicated by Neuman and Kreuger (2003), a response rate of 10 to 50 per cent is common for a mail survey. Sandford and Hasseldine (1992) achieved a response rate of 39.8% from employers and 31% from GST registered persons in their survey on tax compliance costs in New Zealand. Their study further showed that responses from small business enterprises were the lowest amongst business groups (Sandford and Hasseldine 1992). Another survey by Hasseldine et al. (1994) achieved a 22% response rate. Recent studies using a random sample of small and medium sized New Zealand enterprises also had a low response rate, usually between 20-25% (Jackson 2000; Tweed and Chen 2006).

It is possible that the relatively low response rate was due to the length of the questionnaire. Tan's (1999) study, which elicited information from business taxpayers, achieved a response rate of about 43%, but the questionnaire was very much shorter[24] than the one used in this study. Additionally, some of the questions posed may be considered by the respondents as sensitive questions. Putting sensitivity aside, most people tend to be less interested in completing questionnaires related to tax than other topics (Ahmed and Braithwaite 2005). Although a high response rate is always ideal, the low response rate achieved in this study is not considered to be too far from the norm achieved for this type of survey in Australasia.[25]

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23 Out of this total, 40 respondents were from the listed companies.

24 The questionnaire consisted of only 12 questions set out in a six-page booklet.

25 For Australian studies, see for example, Mearns and Braithwaite (2001) and Wenzel, Murphy, Ahmed and Mearns (2004).

5.5 Exploratory data analysis

Data cleaning of the survey responses was initially conducted to check for outliers, values outside the range, and missing data, and initial analyses revealed whether or not distributional assumptions for later statistical testing had been met. Of note is that the variables measuring taxpayers' expectations were more skewed than other variables. Most of the skewness, however, falls within the acceptable range of plus or minus one (Leech et al. 2005). These distributions therefore could be considered at least approximately normal. Missing values were also checked and were negligible. The majority of variables had less than 5% ($n \leq 10$) of missing values.

The respondents were divided into two groups to check for nonresponse bias. Those respondents who sent in their questionnaires from the first batch sent out were grouped as early respondents (n = 157), and those who sent their questionnaires in after the reminder were grouped as late respondents (n = 105). This test was carried out as late respondents are usually regarded to be most similar to nonrespondents (Armstrong and Overton, 1977). Mann-Whitney tests were carried out to test for differences in the ordinal data and independent *t* tests were carried for interval data. As a negligible number of variables (9%) showed a significant difference between early and late respondents, the data set is considered free of detectable and systemic response bias. None of the differences between early and late respondents was related to the social demographic characteristics of the respondents.

This finding is reassuring in that it suggests that there is value in looking at this sample of taxpayers in more descriptive detail. This chapter provides a profile of business taxpayers, and the way in which they engaged with practitioners and the advice they gave.

5.6 Content analysis

Content analysis was used to systematically examine the responses to the open-ended questions. Each respondent was allocated a respondent number and his/her responses to each question were skimmed to get a gist of what each was saying. A coding system was used to note those responses that shared similar or consistent ideas and those that did not. These notes were reread to connect and interpret data themes and patterns.

About 58% (n = 152) of business taxpayers responded at least once to the several open-ended questions. Many of the responses were brief, written by the taxpayers to comment on or clarify particular issues raised in the questionnaire. The highest overall number of responses touched on reasons for changing tax practitioners. Next most common were thoughts about their tax practitioners' services. The data that emerged from these open-ended questions were used to help interpret quantitative survey findings. The qualitative data appear throughout the thesis often through the use of quotations. Quotations are accompanied by respondent numbers (RN).

5.7 Business taxpayer profile

Table 5.1 shows the breakdown of the taxpayer sample in terms of business size, business structure, position held, and their practitioners' affiliation with professional bodies.

Table 5.1: Respondents' profile - business taxpayers' firm characteristics and their practitioners' affiliation

	Frequency	%
Full time employees		
0	29	11.4
1- 5	91	35.5
6-19	61	23.1
20-49	23	8.6
50-99	16	5.9
100+	42	16.5
	262	100.0
Turnover		
Up to $40000	13	5.1
>40000-$100,000	18	7.1
>$100,000- $500,000	56	22.0
>$500000 - $1 million	26	10.2
>1 million-5 million	65	25.6
>5 million-$20 million	30	11.8
>$20 million - $50 million	46	18.1
	254	100.0
Business structure		
Sole proprietor	30	11.5
Company	209	80.4
Partnership	18	6.9
Other	3	1.2
	260	100.0
Position in firm		
Director	87	33.6
Owner-manager	76	29.3
CEO/CFO	24	9.2
Accountant	21	8.1
Financial Controller	29	11.2
Partner	9	3.5
Other	13	5.0
	259	100.0
Practitioners' affiliation		
Big 4 CA firm	75	28.7
A local or regional CA firm	174	66.7
A non CA firm	6	2.3
An attorney/law firm	6	2.3
	261	100.0

5.7.1 Size of business

The majority of the business taxpayers were from firms that employed not more than 20 full time employees. About 70% of taxpayers were from SMEs (fewer than 20 employees), of which 47% were from microenterprises. In terms of turnover, the vast majority (70%) of business taxpayers came from firms with an annual turnover of not more than $5 million. This profile shows that although respondents represented different sized businesses, the majority were from small and medium businesses as expected.

As firm size was used as a control variable, the firms were dichotomised in accordance with the national statistics classification of SME sized enterprises. Those with fewer than 20 employees were coded as 1 to represent SME. Those with 20 or more employees were coded as 2 to represent large firms. Accordingly, the SMEs comprised 70% (n = 181) and the large businesses comprised 30% (n = 81) of the sample.

5.7.2 Business structure, position held, and affiliation with professional bodies

With regard to business structure, most respondents' businesses (80%) were structured in the form of companies. Out of 209 companies, 41 (20%) were listed companies. As for partnerships, one (7%) had three to five partners while the remainder had one to two partners. The other businesses were, in the main, sole proprietorships (almost 12%).

New Zealand business statistics for 2006 showed that 52% of businesses were carried out in the form of companies, 22% sole proprietorships, 13% partnerships and 13% under other categories (for example, government departments). In comparison, the sample in this study comprised a much higher proportion of companies and a lower proportion of partnerships and sole proprietorships. This is likely to reflect the criteria (or sample selection) in part. The sample under study here involved only those who had engaged a tax practitioner. It is very likely that the 78 taxpayers who indicated that they did not engage the services of a tax practitioner were structured as sole proprietorships or partnerships. Moreover, special attention was given to sampling large companies because of concerns that they would be underrepresented in the final sample.

With regard to their position within the firm, the majority of the respondents (63%) were either company directors or owner-managers of the firm. About two thirds of the businesses employed a local or regional Chartered Accountant (CA) firm to help them with their tax work and about 29% used a Big 4 CA firm.

Table 5.2 provides a breakdown of the business taxpayers' use of a tax practitioner, and familiarity with tax matters and taxation authorities.

5.7.3 Use of tax practitioner

About 42% of the business taxpayers had used the services of their current practitioner for five years or less, 27% for six to10 years, 22% for 11 to 20 years, and 9% for more than 20 years. This profile shows that more than half of this sample of business taxpayers had established a good long-term working relationship with their practitioners. A majority of taxpayers (60%) did not use their practitioners' firm for nontax services. Among those who did, most sought business advisory services (21%) followed by audit services (13%). Further investigation of this group who used other services revealed that it was mainly the SMEs that sought business advisory services whereas the large enterprises sought audit services.

5.7.4 Engagement letter

About 59% of the business taxpayers did not receive an engagement letter from their practitioners' firm specifying the work to be performed, the security, and confidentiality of private and personal information and the cost of the tax services. This is rather surprising since most of the practitioners serving the business taxpayers were Chartered Accounting firms. One would expect that these professional firms would want to spell out their terms and conditions with their clients to safeguard their firms. It is possible that some of these firms might have received a letter from their practitioner specifying the terms but were not aware that the letter is termed an 'engagement letter', or perhaps over time they had simply forgotten and had no reason to search for it.

Table 5.2: Respondents' profile - business taxpayers' use of practitioner, knowledge, and audit and penalty experience

	Frequency	%
No of years with current practitioner		
1- 5	108	42.0
6-10	69	26.9
11-20	57	22.4
>20	23	8.7
	257	100.0
Use of other services		
No	157	59.9
Audit	35	13.4
Business advisory	54	20.6
Other services	6	2.3
Combination of the above	10	3.8
	255	100.0
Received engagement letter		
Yes	151	59.4
No	103	40.6
	254	100.0
Level of tax knowledge		
Very low	8	3.1
Low	46	17.7
Medium	150	57.7
High	48	18.5
Very High	8	3.1
	260	100.0
Familiarity with penalties		
Very low	12	4.7
Low	78	30.2
Medium	113	43.8
High	45	17.4
Very High	11	3.9
	258	100.0
Experience of tax penalties*		
Late filing penalty	60	23.7
Late payment penalty	91	35.4
Shortfall penalty	26	10.4
Non electronic filing penalty	3	1.2
Experience of IRD audit		
No	120	46.2
Once	84	32.3
More than once	56	21.5
	260	100.0

*shows respondents who indicated that such a penalty had been imposed on their firm in the last three years

5.7.5 Level of tax knowledge and familiarity with tax penalties

The tax literature indicates that taxpayers' knowledge about taxes is generally poor (Kirchler 2007). In order to ascertain the respondents' level of tax knowledge, two items were used measuring tax knowledge in general and familiarity with tax penalties as follows:

> Overall, how do you rate (a) your own level of tax knowledge and (b) your familiarity with tax penalties?

A rating scale of 1 = "very low" to 5 = "very high" was used for these two measures. The vast majority of taxpayers reported they had at least a medium level of tax knowledge (*M* = 3.0; *SD* = .78) and some familiarity with tax penalties (*M* = 2.9; *SD* = .89). This finding shows that business taxpayers, unlike taxpayers in general, have a fair bit of tax knowledge and therefore provides some assurance that those who responded should have understood the various tax issues raised in the questionnaire.

5.7.6 Experience with tax penalties and IRD audit

The most common experience of a penalty by the firms was a late payment penalty (reported by 35%) followed by a late filing penalty (reported by 24%). A significant portion of respondents had experiences with the New Zealand Inland Revenue Department (IRD) that had resulted in the imposition of a fine. Possibly reliance on a tax practitioner is a way of avoiding future trouble for at least some of the taxpayers.

5.7.7 Audit experience

There was variation in the sample in terms of experience with an IRD audit. Slightly more than half (54%) of the business taxpayers had been audited at least once by the IRD (32% of the respondents had been audited once and 22% more than once). As audit experience is used as a control variable, the results were dichotomised so that "1" represented those who had not been audited before (46%) and "2" represented those who had been audited (54%).

5.8 Business taxpayers' approach to tax advice

5.8.1 Preference for type of tax advice and readiness to acquiesce

Information from business taxpayers about their working relationships with practitioners was elicited. Of interest were their style of communication with their practitioner, the type of advice they wanted and the extent to which they acquiesced to their practitioner's advice. The descriptive statistics (see Table 5.3) showed that 34% of taxpayers assumed that their practitioners knew their preferences and 40% indicated that they made their preferences explicitly clear to them. Another 22% indicated that they let their practitioners decide what was best for their firm irrespective of their personal preferences. This latter group appeared to rely heavily on practitioners as 'the tax experts', which is consistent with results from the qualitative study recently conducted by Ashby and Webley (2008) where the very small business sector in the UK also indicated that they just leave it to their accountant to sort it out for them. Overall, these data support the view that different groups of taxpayers have different ways of communicating with their practitioners regarding the type of advice which they prefer.

Table 5.3: Distribution of business taxpayers' preferences for type of tax advice

	n	%
I assume they know my preferences	86	34
I make my preferences explicitly clear to them	103	40
I let my practitioner decide what is best for my firm	56	22
Other*	11	4
Total	256	100

* Other represents a combination of the first three types of preferences

Furthermore, as shown in Table 5.4, the vast majority (85%) indicated that they frequently accepted whatever advice was given. Almost all taxpayers (96%) indicated that they would also discuss alternative measures. About 64% indicated that they had expressed, on occasion, disappointment with the recommendations received. It is interesting that, the majority (61%) indicated that they had occasionally checked the advice out with someone else. These findings indicate that the course of action taken by taxpayers following advice from their practitioner varies, perhaps depending on the context. As some respondents commented, their course of action might depend on the amount of tax savings under consideration. If the amount were immaterial, they would most likely accept whatever advice was given. However, if the amount were material, they would be more likely to seek a second opinion. Taxpayers' decisions, therefore, can be seen to involve a cycle of role sending and responding on the part of both practitioner and client as depicted in the Tax Practitioner-Client Role Model. In the words of a respondent from a small business who never accepts whatever advice is given by the practitioner: "the whole exercise should be a mutual teaching learning experience for both parties and dialogue is important" (RN 238). According to another respondent from a listed company, whose practitioner is from one of the Big 4 CA firms: "Up and down, all firms can typically provide good advice. It then comes down to relationships and the ability to work together" (RN 225).

These findings provide insight into how the interactions are most likely to proceed. Most times, taxpayers acquiesce. Occasionally, however, they express dissatisfaction, seek advice elsewhere, and discuss alternatives. There is indeed a more dynamic exchange going on in their working relationship than prior studies have managed to capture.

Table 5.4: Distribution of business taxpayers' readiness to acquiesce (n ranges from 240 to 251)

Approaches	Never	Occasionally	Frequently
Accept whatever advice is given	3.2%	11.6%	85.3%
Discuss alternative measures	4.0%	55.5%	40.5%
Express disappointment with recommendations	36.3%	60.0%	3.8%
Check advice with someone else	38.6%	58.1%	3.3%

5.8.2 Disclosure of information to practitioners

For practitioners to assist their clients with tax compliance, they would need them to disclose all tax-related information held by the firm. However, clients may not always disclose all information. The majority of the respondents in this study indicated that they disclosed all the necessary information (94%). This response suggests that most taxpayers are open and honest with their practitioners. It is interesting to note some of the reasons offered by those respondents who indicated that they did not disclose everything:

- "he does not need to know everything." (RN 26 – from a very small firm).
- "because sometimes the practitioner is too keen to follow the letter of the law." (RN 50 – from a very small firm).
- "immaterial and would be costly alerting them to the IRD." (RN 52 – from a very small firm).
- "relevance, materiality, and time constraints in dealing with too much detail." (RN 74 – from a large company with a practitioner from one of the Big 4 firms).
- "not his responsibility, can't get into trouble if they don't know." (RN 107 – from a very small firm).
- "lack of time/opportunity to communicate." (RN 133 – from a medium sized firm).
- "he is not up to speed so need not know." (RN 150 – from a small firm).
- "like to retain control internally and only get advice involved or required." (RN 225 – from a listed company with a practitioner from one of the Big 4 firms).
- "we have minimal contact, can't be bothered." (RN 256 – from a very small firm).

Not disclosing information does not necessarily mean that they are underreporting income or overstating deductions, intentionally or unintentionally, although these possibilities also cannot be completely ruled out. It does suggest, however, that a minority of business taxpayers maintain tight control over their financial decision making.

5.8.3 What constitutes aggressive advice?

As taxpayers may have perceived aggressiveness quite differently, their perceptions regarding various interpretations of aggressive advice were elicited. A rating scale of 1 = "strongly disagree" to 5 = "strongly agree" was used for this measure. As shown in Table 5.5, the mean score for each of the nominated interpretations of aggressive advice was more than 3. The highest percentage agreement were: favours a taxpayers' tax position (73%), followed by not upheld if challenged by court (68%), goes against intent of law (68%), higher chance of failure (65%), involves contrived arrangements (60%) and involves non-commercial arrangements (54%).

Table 5.5: Means and standard deviations (SD) for what constitutes aggressive advice by business taxpayers (n ranges from 241 to 251)

Aggressive advice refers to advice that:	M	SD
1. Favours a taxpayer's tax position on a questionable item	3.7	.83
2. Involves arrangements which are contrived and artificial in their method of execution	3.6	1.25
3. Involves arrangements which are not commercial from a business or economic perspective	3.5	1.18
4. Has a higher chance of failure than success if challenged by IRD	3.7	1.12
5. May not be upheld if challenged by court	3.7	1.07
6. Goes against policy intent of tax law but still within letter of law	3.7	.93

This indicates that the majority of taxpayers agreed that these types of advice were considered as aggressive. It is interesting to note that taxpayers agreed that any advice that goes against the policy intent of the tax law is also aggressive advice. These views are generally consistent with the literature and with the views of the tax practitioners (see discussion in Chapter 7).

5.9 Core research concepts and their measurement

This section describes how the conceptual design was operationalised. It includes how the following core concepts were measured in the survey: expectation-experience gap, satisfaction, practitioner retention, trust, personal and business tax ethics, risk propensity, sanction risk perception. Multi-item scales were developed where possible to increase the reliability and validity of the measures.

5.9.1 Expectations and experiences of tax services

As taxpayers may have different expectations of and experiences with their practitioners, the following seventeen measures of expectations were used in this study:

1. Help my firm file an accurate return;
2. Help my firm minimise tax;
3. Help my firm avoid serious penalties;
4. Explain the tax law and regulations using words that I/we understand;
5. Know many ways to save taxes;
6. Be able to exploit tax loopholes to the advantage of my firm;
7. Be creative in dealing with my firm's tax matters;
8. Reduce uncertainties in tax matters that concern my firm;
9. Be up to date with the latest changes in tax law;
10. Save my firm considerable time in dealing with tax matters;
11. Advise my firm not to take deductions that fall within any grey areas of the tax law;
12. Be clear about the risks associated with the recommended advice;
13. Provide my firm with conservative advice in areas where the tax law is not ambiguous;
14. Provide my firm with aggressive advice in areas where the tax law is ambiguous;
15. Promote any tax effective schemes to my firm so that I/we don't have to pay too much tax;
16. Assist my firm to make claims only when they are clearly legitimate;
17. Just deal with my firm's tax matters with minimum fuss and without bothering us too much with it.

This list of expectation statements was drawn up after reviewing the literature, with some adaptation from the work of Braithwaite (2000), Chang and Bird (1993), Christensen (1992), Collins et al. (1990), and Hite et al. (1992).

To enable comparison between what taxpayers expected and experienced from practitioners' services, the experience statements were based on the same 17 items mentioned above. Some phrasing was slightly different in order to measure experience rather than expectation. A scale from 1 = "strongly disagree" to 5 = "strongly agree" was used for rating each item in terms of expectations and experiences.

Table 5.6 shows the means (M) and standard deviations (SD) for expectations and experiences. Out of the 17 items, nine types of expectation had a mean score of 4.5 or higher. Most importantly, taxpayers expected their practitioners to be up to date with changes in the tax law. This finding is not surprising as in recent years the government has reformed various parts of tax law. Undoubtedly, every taxpayer who seeks the assistance of a tax practitioner would like one who is up to speed with tax law changes; otherwise their other expectations may not be met! The next most essential service after being up to date with changes in tax law are filing an accurate return, minimising tax and avoiding serious penalties which appear to be most important to them. These findings are consistent with those from prior studies, which suggest that these considerations are important motivators for engaging the services of a tax practitioner (for example, Collins et al. 1990; Hite et al. 1992).

Table 5.6: Means (SD) for business taxpayers' expectations and experiences (n ranges from 250 to 262)

Items	Expectation Mean (SD)	Experience Mean (SD)
1. File accurate return	4.7 (.47)	4.4 (.61)
2. Minimise tax	4.7 (.56)	4.0 (.84)
3. Avoid tax penalties	4.7 (.56)	4.2 (.74)
4. Explain the tax law & regulations clearly	4.6 (.58)	4.1 (.81)
5. Know many ways to save taxes	4.5 (.65)	3.8 (.84)
6. Exploit tax loopholes	3.8 (1.01)	3.2 (.93)
7. Creative with tax matters	3.9 (1.01)	3.4 (.96)
8. Reduce uncertainties	4.5 (.55)	4.0 (.86)
9. Up to date with the latest changes in tax law	4.8 (.40)	4.3 (.69)
10. Save time in dealing with tax matters	4.6 (.62)	4.0 (.86)
11. Not to take deductions in grey areas of law	3.9 (.96)	3.7 (.89)
12. Mention risks associated with the advice	4.5 (.59)	4.0 (.74)
13. Give conservative advice where unambiguous.	3.7 (1.06)	3.7 (.88)
14. Give aggressive advice where ambiguous.	3.2 (1.10)	3.0 (.97)
15. Promote tax effective schemes	4.1 (.93)	3.4 (.99)
16. Make claims only when clearly legitimate	4.3 (.78)	4.1 (.66)
17. With minimum fuss and not too much bother	3.3 (1.23)	3.6 (1.02)

Two expectations are of note because they had the lowest agreement and highest variation. They are giving “aggressive advice” (*M* = 3.2; *SD* = 1.10) and advising with “minimum fuss” (*M* = 3.3; *SD* = 1.23). About 40% of taxpayers expected their practitioners to provide aggressive advice where the tax law was ambiguous. Consistent with a 40:60 split on aggressive advice was the finding that just over half (52%) agreed that their practitioner should deal with their firms’ tax matters with minimum fuss and not bother them too much with it. It appears that taxpayers are divided on whether their practitioners should be noninterventionist and whether they should offer aggressive advice. Clearly, there is no agreed norm for this sample of taxpayers. That said, the correlation coefficient between what clients wanted and what they experienced were relatively high. On aggressive advice, the correlation between expectation and experience was 0.53 ($p < .001$). On minimum fuss, the expectation-experience correlation was even higher ($r = .62$; $p < .001$). This ‘pleasant surprise’ was not anticipated on the basis of previous research, but explains a basic benefit experienced by clients in their relationship with practitioners. Overall, these findings suggest that taxpayers found practitioners who suited their requirements.

5.9.2 Dimension of business taxpayers’ expectations

The 17 kinds of expectations that taxpayers had of practitioners, while interesting in their own right, were likely to be unwieldy for hypothesis testing later on. Therefore, a decision was made to reduce them to a limited set of dimensions. A principal component factor analysis with varimax rotation was carried out to uncover the key dimensions of taxpayer expectations. Since the purpose of factor analysis is to account for associations between variables, the initial correlation matrix (*R*-matrix) was inspected to identify variables that were not correlated with others. Two items of expectations, that is, “minimum fuss” and “conservative advice” did not have at least one correlation of the order of .3 with other items. Because of their low shared variance with other items (low communalities), they were removed from the item set (Kinnear and Gray 2006). The factor analysis was re-run and produced three factors with eigenvalues greater than one, accounting for 57% of variance in the item set (see Table 5.7).

After rotation, the results revealed three distinctive dimensions of expectations. The results of the analysis appear in Table 5.7. The first factor, "Technically Proficient", included nine types of expectations which centred on the technical proficiency or competency of the practitioner. Examples of technical proficiency from Table 5.7 are being up to date with changes in tax law, file accurate tax return, know ways to save tax, and save time. The second factor, "Aggressive Advice", was composed of four types of expectations which signified aggressive postures including exploiting tax loopholes and promoting tax schemes Two items, representing taxpayers' preference to remain cautious and not play with grey areas of tax law comprised "Cautious Advice".

Table 5.7: Factor loadings from a principal component analysis and varimax rotation for business taxpayers' expectations of practitioners

Expectations	Factor 1 Technically Proficient	Factor 2 Aggressive Advice	Factor 3 Cautious Advice
Up to date with latest changes in tax law	.760		
Avoid tax penalties	.726		
File accurate return	.697		
Reduce uncertainties	.661		
Explain tax law & regulations clearly	.635		
Minimise tax	.595		
Save time in dealing with tax matters	.588		
Mention risks associated with advice	.579		
Know many ways to save taxes	.535		
Creative with tax matters		.816	
Exploit tax loopholes		.812	
Give aggressive advice where ambiguous		.740	
Promote tax effective schemes		.616	
Not to take deductions in grey areas of law			.801
Make claims only when clearly legitimate			.780
Explained variance (before rotation)	25%	19%	12%

The items defining each factor in Table 5.7 were used to develop scales representing technically proficient expectations, aggressive advice expectations, and cautious advice expectations. A mean score was obtained for each scale by summing responses to the items under each factor and dividing the total by the number of items in the scale to bring the scores back to their original item metric of 1 to 5.

Table 5.8 shows the scale means (*M*) and standard deviations (*SD*), scale inter-correlations and scale Cronbach's alpha. The scales used to measure expectations were the model for constructing scales to measure experiences. The internal consistency coefficients (Cronbach's alpha) for the technically proficient and aggressive advice scales were stronger than that observed for the cautious advice scales. Given that the cautious advice scales had only two items, the alpha coefficient is considered strong (Field 2005). Of particular note is the way in which scales representing technically proficient, aggressive advice and cautious advice are positively correlated, more so for experiences than for expectations. These findings suggest that taxpayers see no inconsistency in expecting all these qualities in their practitioners. Moreover, their experiences suggest that these qualities coexist in tax practitioners.

Table 5.8: Means, SDs, Pearson intercorrelations, and alpha reliability coefficients (Cronbach's alpha) for business taxpayers' expectations and experiences

	Mean	SD	1	2	Cronbach's alpha
EXPECTATIONS					
1. Technically proficient	4.62	.38	-		.864
2. Aggressive advice	3.75	.79	.414***	-	.777
3. Cautious advice	4.13	.74	.476***	.273***	.619
EXPERIENCES					
1. Technically proficient	4.07	.57	-		.885
2. Aggressive advice	3.24	.75	.593***	-	.790
3. Cautious advice	3.90	.67	.645***	.397***	.644

*** $p < .001$

Overall, taxpayers' priorities were for their practitioners to be technically proficient and provide cautious advice with aggressive advice lagging behind. This pattern described experiences as well as expectations. An implication of these results is that although taxpayers want to be cautious, that is, they want their practitioners to 'play safe', they are also open to aggressive advice. It appears that, ideally, they do not want to miss any opportunity to minimise tax within the letter of the law. This finding is consistent with those from the study conducted by Sakurai and Braithwaite (2001) which showed that taxpayers who looked for a tax practitioner who minimised tax without conflict would also consider one who did the job more aggressively.

These three distinct dimensions of expectations and experiences were used as the dependent variable for testing hypotheses 1 and 2 in Chapter 6, that is, there will be a gap between taxpayers' expectations and experiences, and the gap will predict satisfaction and retention of practitioner.

5.9.3 Satisfaction with and retention of tax practitioner

Taxpayers' satisfaction with, and commitment to, their current practitioner were measured by asking respondents to indicate their agreement with the following statements:

(a) Overall, I am satisfied with my tax practitioner's services;
(b) I will continue to use the same tax practitioner again for my firm next year.

The rating scale used for responses to each statement was 1 = "strongly disagree" to 5 = "strongly agree". These concepts were adapted from Christensen's (1992) survey questionnaire where she combined the two statements to represent a measure of satisfaction.

Table 5.9 shows the means (*M*) and standard deviations (SD) for overall satisfaction with practitioners' service and for retention. In both cases, the means exceeded 4 on a 5-point scale indicating that the majority were satisfied with their practitioner and would retain the services of their practitioner again next year.

Table 5.9: Means, SDs, and Pearson intercorrelations for two measures of business taxpayers' satisfaction - overall satisfaction with services and retention of practitioner (n = 262)

Satisfaction Measures	% Agree	M	SD	1	2
1. Overall satisfaction	86%	4.01	.97	-	
2. Retention	90%	4.12	.70	.707***	-

*** $p < .001$

The association between these two variables, as indicated by the Pearson correlation coefficient, was strongly significant and positive. The results showed that those with a high level of satisfaction were more likely to express willingness to retain their practitioners' services. Accordingly the two items were summed and averaged to arrive at a single scale labelled 'satisfaction' denoting the combined outcome of satisfaction with services and retention of services (*M* = 4.1; *SD* = .67; *alpha* = .827). This scale was used to test Hhypothesis 2 in Chapter 6, that is, if taxpayers' experiences do not match their expectations of practitioners' services, they will consider practitioners' services as unsatisfactory.

5.9.4 Trust in practitioner

As depicted in the Tax Practitioner-Client Role Model, interpersonal relations between the practitioner and client are crucial to the relationship. This study was focused on trust as the measure of quality of interpersonal relations. Taxpayers' trust in their practitioner was measured by using a 4-item scale, which was adapted from Braithwaite (2001):

My tax practitioner:

1. Is open and honest with me in dealing with my firm's tax matters;
2. Is a trustworthy person;
3. Acts in the interest of my firm rather than his/her own interests;
4. Has high integrity.

The items were rated on a 5-point Likert scale ranging from 1 = "strongly disagree" to 5 = "strongly agree".

More than 90% of taxpayers indicated that their practitioner was open and honest, trustworthy, and had high integrity. About 85% of taxpayers perceived their practitioners to act in the interests of their firms. This finding is also well supported by the following comments received from taxpayers:

- "despite my accountant not meeting some expectations, he provides a reliable and trustworthy service and knows our business well." (RN 257 – a respondent who expressed satisfaction with, and trust in, the practitioner).
- "we have total confidence in our tax practitioner and have an open relationship where anything can be discussed" (RN 92 - a respondent from a SME who is very satisfied with, and fully trusted the practitioner).

Table 5.10 shows the Pearson's product-moment correlations for the items in the trust scale. The correlations, which ranged from moderately strong to strong, were all statistically significant.

Table 5.10: Means, SDs, and Pearson intercorrelations for trust (n = 262)

Trust Measures	M	S.D.	1	2	3	4
1. Is open and honest	4.48	.58	1.00			
2. Is trustworthy	4.51	.57	.80**	1.00		
3. Acts in firm's interest	4.21	.81	.63**	.63**	1.00	
4. Has high integrity	4.46	.62	.70**	.76**	.73**	1.00

** $p < .01$

A reliability analysis was performed on the four items of trust. Cronbach's alpha was .90 indicating that the 4-item scale was reliable in terms of internal consistency. Accordingly, responses to the four items were summed and averaged to obtain for each taxpayer a single scale score for trust (M = 4.42; SD = .57). The trust scale was used to test Hhypothesis 3: taxpayers' trust in their practitioners will be positively associated with their satisfaction with practitioners' services.

5.9.5 Agreement with advice

One of the aims in this study was to examine the factors that affect taxpayers' reporting decisions in an ambiguous setting (income and expense) as this is an area which has potential for practitioners to exploit the tax law to their clients' advantage (see Klepper and Nagin 1989). The close match of taxpayers' expectation and experience in the giving of conservative advice when the tax law is unambiguous (as shown in Table 5.6), lends further support for this study to be focused on taxpayers' behaviour when their practitioners recommend aggressive advice in areas where tax law is ambiguous.

Although legal ambiguity is an important factor in tax reporting decisions, it is not feasible to consider all types of ambiguous tax issues in one questionnaire. As a result, two generic hypothetical scenarios, one concerning deductions and the other concerning classification of income, were provided to examine taxpayers' tax reporting decisions and whether decisions will be different in different contexts. Hypothetical scenarios were used to avoid self-report bias as some participants may have considered these issues to be 'sensitive.' The scenarios were therefore used as an indirect measure of taxpayers' tendency toward aggressive tax reporting decisions.

Long and Swingen (1991:646) noted that ambiguity exists at three levels. There are ambiguity and uncertainty in the precise meaning of the statutory language, in determining how the law specifically applies to an individual situation and in the type(s) of evidence sufficient to establish that the alleged facts are true. Taking these features into consideration, the first scenario that involved an ambiguous area in tax deduction was stated as follows:

> Say your firm has incurred an expense of a **considerable** sum and you seek your tax practitioner's advice as to whether the expense is deductible. Your practitioner tells you that the tax law relating to this expense is **rather ambiguous** but thinks that it should be deductible. However, if the deduction is challenged by the IRD, your practitioner tells you that there is a 50% chance that it may not be upheld by the court in your favour. If your practitioner advises you **to claim** the deduction in your firm's tax return, will you agree with his/her advice?

The second scenario mirrored that of the first scenario but it involved an ambiguous area in the classification of income and was stated as:

> Say your firm has received a considerable amount of income and you seek your tax practitioner's advice as to whether the income is taxable. Your practitioner tells you that the tax law relating to this type of receipt is **rather ambiguous.** It is arguable as to whether the income is of a capital (non-taxable) or a revenue nature (taxable), but your practitioner thinks that it should be regarded as capital. However, if this income is challenged, your practitioner tells you that there is a 50% chance that it may not be upheld by the court in your favour. If your practitioner advises you to regard the income as **capital**, will you agree with his/her advice?

These two scenarios were adapted from Braithwaite (2000), Christensen and Hite (1997), Hite and McGill (1992), and Tan (1999). The chance that it will not be upheld by the court was stated as 50% to depict an element of uncertainty. Since both scenarios are ambiguous and the practitioner's advice is pro-taxpayers, the advice given is considered of the aggressive type. This categorisation is in accord with taxpayers' interpretations shown in Table 5.5 where most agreed that aggressive advice involved favouring a taxpayer's tax position on a questionable item which may not be upheld if challenged by the court.

The amount under consideration could also have an impact on taxpayers' tax reporting decisions. When amounts are trivial, taxpayers may not be too concerned about the consequences of their decisions. However if the amount is considerable, other factors may come to bear on the taxpayers' decisions as they are likely to consider more carefully the consequences of their decisions. In both scenarios above, therefore, it was stated that the amount of expense and income is considerable.

A rating scale from 1 = "definitely no" to 5 = "definitely yes" was used to measure the extent of taxpayers' agreement with their practitioner's aggressive advice. Their agreement or disagreement with their practitioner's advice in the hypothetical scenarios represented the dependent variable.

As displayed in Table 5.11, the mean scores show a greater tendency to agree than disagree with practitioners, with both means above the midpoint.[26] There appears to be higher agreement with practitioners' aggressive income advice (*M* = 3.52; *SD* = .94) than deduction recommendation (*M* = 3.48; *SD* = 1.02). However, the result of a paired samples *t* test shows that there was no significant difference in taxpayers' responses to the deduction and income situation (t = -0.851, p = .396, 2-tailed).

To test the realism of the described tax scenarios, taxpayers were also asked whether they had experienced such a situation before. Actual experience with such a scenario would support the validity of the scenario. About 21% (n = 55) of the respondents indicated that they had experienced such a deduction situation. For the income situation, about 15% (n = 40) of respondents had experienced such a situation. The scenarios, although hypothetical, therefore appeared to resonate with experience and were considered reflective of real situations.

Table 5.11: Means, SDs, for agreement with practitioners' advice on ambiguous deduction and income items (n ranges from 258 to 259)

Taxpayers' response	M	SD
Agree with aggressive advice on ambiguous deduction item	3.48	1.02
Agree with aggressive advice on ambiguous income item	3.52	0.94

The association between the deduction situation and the income situation, as indicated by the Pearson correlation coefficient, was strongly significant and positive (r = .67, p < .001). That is, those who accepted aggressive advice on income were also likely to accept aggressive advice on deductions. Accordingly, the responses to the two scenarios were summed and averaged to produce a single scale representing agreement with aggressive advice (*M* = 3.56; *SD* = .856; *alpha* = 0.797).

5.9.6 Expectation of aggressive advice

As observed previously (see Table 5.6), the mean and standard deviation scores (*M* = 3.2; *SD* = 1.10) suggest variability in opinions about how taxpayers approach aggressive

[26] About 61% agreed with the deduction situation and 63% agreed with the income situation.

advice where tax law is ambiguous. However, the single item measure, expectation of aggressive advice (item 14 as shown in Table 5.6) was correlated with three other measures of aggressive advice shown in Table 5.7. Consequently, the scale based on expectation of aggressive advice in the factor analysis (made up of four-items) was considered the more appropriate measure as the independent variable to test Hhypothesis 4; that is, taxpayers who expect aggressive advice tend to agree with their practitioners' recommended aggressive advice. As shown in Table 5.8, the mean for this scale was 3.75 and standard deviation .79 (*alpha* = .78).

5.9.7 Personal and business tax ethics

Because of concerns that some business taxpayers may want to present an artificially pro-social image of their personal ethics (Hite et al., Stock and Cloyd 1992), an attempt was made in this study to measure personal ethics by eliciting the information in a more indirect manner. The question asked was:

> Do you think your firm should declare all taxable income in the tax return?

This measure was adapted from Wenzel's (2002) work and was used to test Hhypothesis 5, that is, personal tax ethics will have an effect on their agreement with practitioners' aggressive advice. The rating scale from 1 = "definitely no" to 5 = "definitely yes" was used to measure this norm.

A huge majority (91%) responded affirmatively (M = 4.26; SD = .72). In comparison, Braithwaite et al.'s (2001) results showed that 72% of taxpayers agreed that they should honestly declare their cash earnings. Hite et al. (1992) had 75% who indicated that they never knowingly failed to report income. This group of respondents therefore saw themselves as highly ethical although there is a possibility of socially desirable responding. Possibly other items in the survey about approaches to aggressive advice made them particularly sensitive. Another possibility is that strictly following the letter of the law has gained support precisely because there are so many possibilities for playing with grey areas of law which open opportunities for tax avoidance. If taxpayers can avoid, and do so legally in their own eyes, then there is no need for them to engage in tax evasion.

Business tax ethics were measured by asking taxpayers their perceptions of what they thought other business firms would ask their practitioners to do to help them minimise taxes. An 8-item scale was used as follows:

1. Exaggerate deductible expenditure;
2. Underreport taxable income;
3. Manipulate accounts receivable;
4. Manipulate accounts payable;
5. Manipulate inventory figures;
6. Claim private expenses as business expenses;
7. Claim capital expenses as revenue expenses;
8. Manipulate work in progress figures.

Some of these items were adapted from Attwell and Sawyer (2001). The requests generally depict unethical or aggressive types of requests. The rating scale used for these measures of business tax ethics ranged from 1 = "never" to 4 = "frequently".

Table 5.12: Means, and SDs for items in the perceptions of business tax ethics scale (no. ranges from 246 to 248)

Practitioners helped other firms to	Occasionally%	Frequently	M	SD
1. Inflate expenditure	42	7	2.48	.72
2. Understate income	43	3	2.37	.71
3. Manipulate accounts payable	32	2	2.26	.71
4. Manipulate accounts receivable	31	3	2.23	.72
5. Manipulate inventory figures	37	8	2.44	.75
6. Claim private expenses as business	37	19	2.69	.85
7. Claim capital expenditure as revenue	39	10	2.53	.76
8. Manipulate work in progress	36	20	2.49	.75

The results in Table 5.12 show how this sample of business taxpayers perceived other business firms' tax ethics. While all eight requests appeared to occur, the statistics suggest that they were thought to be made occasionally but not frequently. Claiming private expense as a business expense (37% mentioned "occasionally" and 19% mentioned "frequently"), and capital expenditure as revenue (39% mentioned "occasionally" and 10% mentioned "frequently") were the two most common bases for departure from ethical standards perceived to be made by other firms. A Cronbach's alpha of .90 was calculated for the eight types of requests indicating that they were consistently recognised as measures of ways to minimise taxes. Accordingly, the mean scores for the eight requests were averaged to derive a single scale for business tax ethics (M = 2.45, SD = .57). This scale was used as an independent variable to test Hhypothesis 6, that is, taxpayers' perceptions of usual business tax ethics will influence their agreement with practitioners' aggressive advice.

As a particular practitioner will serve a range of clients, and competing firms may have other practitioners, it is important to examine the views of respondents regarding the kinds of requests likely to be accommodated. If they perceive that most practitioners would not help other firms with such requests, they may conclude that a social norm of honesty or caution is operating. Tax practitioners may be seen as gatekeepers preventing tax abuses. To examine this further, taxpayers were asked whether they thought that the practitioners serving other firms would help them with any one of the eight requests to reduce tax:

> If you are aware that some firms ask their practitioners to help them with one or more of the above, how likely do you think it is that their practitioners will help them?

A rating scale of 1 = "very unlikely" to 5 = "very likely" was used to measure these perceptions. Those who were not aware were not required to respond to this question.

In addition, taxpayers were asked the following question:

> Say if you ever asked your practitioner to help your firm to exaggerate expenditure, how likely do you think it is that your practitioner will help you with your request?

Again, a rating scale of 1 = "very unlikely" to 5 = "very likely" was used for responses.

Table 5.13 shows that taxpayers perceived that their practitioners were more unlikely to help them with those requests as compared to other firms' practitioners. Even then, the perception of the likelihood of assistance from other firms' practitioners was low. The findings suggest that taxpayers perceived practitioners as having integrity to prevent abuse of the tax system.[27] Responses received from some business taxpayers indicated that they would never ask their practitioners to help with such requests in the first place, as what they are interested in is to pay the minimum tax within the law. It is also possible that some of them have no knowledge of other practitioners' practices as there were quite a number (34%; *n* = 90) who did not respond to this question.

Table 5.13: Means, and SDs for likelihood of practitioners' help with requests relating to unethical ways of minimising taxes

Help with requests	Mean	SD
Other taxpayers' practitioners will help with those requests	2.83	.97
Your practitioners will help you with those requests	1.76	.82

Taxpayers' understanding of business tax ethics was further gauged by posing to them the following question:

> Do you think other firms honestly declare all their taxable income in their tax returns?

This measure was also adapted from Wenzel's (2002) work on social norms and rated by using a scale of 1 = "definitely no" to 5 = "definitely yes".

About 35% of taxpayers did not think that other firms honestly declared all their taxable income in their tax returns. In comparison, only about 17% of taxpayers thought that others did and the rest had no idea about other firms' attitudes toward reporting all income. This finding is comparable to Braithwaite et al.'s (2001) Community, Hopes, Fears and Action Survey, which showed that only 20% of Australian taxpayers believed that others honestly declared their cash earnings.

[27] This insight of taxpayers who do not believe other tax practitioners gave in to their clients is interesting. Perhaps this belief probably is in part set up by their own practitioners who could have indicated to them that they would not help with those requests and that very likely most other practitioners would not do so either.

These results show taxpayers perceiving a substantial amount of unethical taxpaying behaviour among business taxpayers but not among practitioners. As some respondents commented:

- "Practitioners have good standing with the IRD and would not jeopardize our relationship with the IRD to meet the needs of one single client." (RN 257 – from a medium sized firm).
- "Neither would they compromise their reputation as Chartered Accountants." (RN 261 – from a medium sized firm).
- "Practitioners are generally honest and law abiding and would not take stupid risks." (RN 104 – from a large firm).

Possibly some business taxpayers were concealing their taxable income from their tax practitioners. A taxpayer (RN 5) from a very small firm who often disclosed all business information to his/her practitioner pointed out that: "if the business was manipulating the figures, they would do so without their tax practitioner's knowledge." This view is shared by another taxpayer also from a small firm (RN 133) who indicated that, "often these are in the everyday expenses and hidden or accounted for before, or at an earlier stage, than the tax practitioner stage". As noted in Section 5.7 on disclosure of information, some taxpayers did not disclose all information regarding their firm's tax matters to their tax practitioners.

5.9.8 Personal risk propensity

Risk propensity is a person's general tendency to take or avoid risk or the likelihood that s/he will engage in a particular activity. This concept (adapted from Hite et al.'s 1992 study) was measured by asking taxpayers the following question:

> Say your firm has incurred an expense of **$300**, and the tax law on the deductibility of this expense is rather ambiguous. How certain will you have to be (on a scale of 0% to 100%) that the IRD will allow the deduction before you will make a claim?

Another similar question was asked but the amount indicated was increased from ***$300*** to ***$3,000.*** Taxpayers' responses to these questions would provide an indication of the extent of risk they were willing to take. The two different amounts used were to test whether materiality had any impact on their decisions.

Percentage scores were averaged and a standard deviation was calculated. The mean scores for the immaterial and material amounts were 63 and 69 (on a 1-100 per cent scale) respectively with standard deviations of .23 and .22. These statistics are comparable to the findings of Hite et al., (1992) which showed that small business taxpayers required 70% certainty before they would claim a deduction.

About 57% (*n* = 239) of the respondents indicated that they needed to be more than 50% certain before they would make the $300 claim. As a higher percentage of certainty denotes a lower level of risk propensity, this indicates that slightly less than a majority (43%) of the respondents were the more risk taking type. When the amount of expense was material, that is, $3,000, about 66% (*n* = 166) of respondents indicated that they required more than a 50% level of certainty before they would claim the expense as recommended by their practitioner. While the sum of money had some effect in the expected direction, it was not a major factor in taxpayers' calculations.

The bivariate Pearson correlation between the ratings for certainty for the $300 and $3000 expense claims showed a moderately strong positive relationship (r = .56; p < .001). Since the Cronbach's alpha is .72, the 2-item measures were considered reliable measures of propensity. Accordingly, the taxpayers' responses to the two items were averaged to derive a single scale for risk propensity (*M*= 65.6; *SD* = 20.1).

A mixture of taxpayers who have high and low risk tendencies comprised the sample of respondents in this study. It was interesting to examine whether those who have higher risk tendencies were more willing to accept aggressive advice than those who have lower risk tendencies. The effect of this independent variable on their agreement with aggressive advice was tested in Hhypothesis 7 and is discussed in Chapter 6.

5.9.9 Sanction risk perceptions

Perception of sanctioning risk was measured by using a hypothetical scenario and asking respondents two questions to assess audit probability and the likelihood of severe penalties:

> Say your firm **claimed** an ambiguous deduction of a considerable sum following your practitioner's advice, what do you think are the chances (on a scale of 0% to 100%) that your firm (a) will be **audited** and (b) will face **severe penalties** if the amount is ruled as not deductible?

About 44% (n = 116) of the respondents perceived that there would be a more than 50% chance of audit. As for chance of severe penalties, about 39% (n = 105) of the respondents perceived that there would be a more than 50% chance of severe penalties being imposed. The mean score for audit and penalties was 55 (*SD* = 26.4) and 52 (*SD* = 29.4) respectively. Perceptions of audit risk and severe penalty risk were also positively correlated (r = .47; p < .001). Since the Cronbach's alpha is .7, the two items were combined through averaging scores, thereby producing a reliable measure of the perception of sanction risk (M = 53.5; *SD* = 24.5). This scale was used as an independent variable to test Hhypothesis 8, that is, taxpayers who perceived a low sanction risk will be more agreeable with their practitioners' aggressive advice on an ambiguous tax situation that those who perceived a high sanction risk.

For these questions, personal risk propensity and perception of sanction risk were focused on deduction of expenses and not income. The reason for focusing only on deduction was to prevent the questionnaire from becoming too lengthy, which may have discouraged people from responding. Since there were no significant differences in taxpayers' agreement on income and deduction issues discussed in Section 5.6, it was assumed in this study that taxpayers' risk propensity and sanction risk perceptions with regard to income items were not significantly different from those for expense items.

A summary of all the variables from the business taxpayers' sample that were tested in the Tax Practitioner-Client Role Model are provided in Appendix D.

5.10 Chapter summary

This chapter details the research design and methods used for collecting data for the business taxpayers' role. The instrument used to collect the data was designed to provide information which was as credible and accurate as possible. For instance, to prevent or reduce the occurrence of socially desirable responding, respondents were assured of their anonymity, and no codes were used to identify them. Where concepts were perceived to have more than one dimension, multiple item scales were used to measure the concept. Overall, the majority of the measures were considered reliable as most of them had internal consistency coefficients (Cronbach's alpha) of at least .70. The response rate was 20% and is considered to be in line with those of other studies carried out on small businesses and on taxpayers in Australasia.

The incorporation of open-ended questions generated more detailed data and gave respondents the opportunity to express themselves or clarify their responses. About 58% of business taxpayers responded at least once in the open-ended questions. This showed that the majority of the respondents were keen to provide clarification or make comments on issues raised in the questionnaire. These qualitative data enhanced the interpretation of research findings and provided evidence that often converged with quantitative data, thereby strengthening confidence in the conclusions.

The data collection was conducted nationwide in New Zealand and about 70% of the respondents were from SMEs. A comparison with the statistics disclosed by the Ministry of Economic Development showed that this percentage is lower than the 96% of SMEs as at February 2006. The shortfall could perhaps be explained by the type of sampling used which was not completely random but rather stratified so that a reasonable number of bigger firms could be represented. The sample was also more selective as only those who used the services of a tax practitioner were included. This is an important criterion as the aim in the study was to examine the relationship between the taxpayer and the practitioner.

Most small businesses with not more than 20 employees were structured in the form of companies. Of note is that the respondents (company directors or owner-managers) who participated in the survey were the ones who made the tax decisions for the firm and had a reasonably good knowledge of tax. Therefore, they were in a good position to identify with the issues raised in the survey questionnaire and respond accordingly. Most employed a regional or local CA, although a significant minority (almost a third) used the Big 4 CA firms.

Under half (42%) of the business taxpayers had been with their practitioner for five years or less revealing that most were in stable taxpayer-practitioner relationships. The majority (59%), however, did not have a letter specifying the terms of engagement with their practitioner, suggesting considerable opportunity for negotiating the services to be provided. Without a letter specifying clearly the clients' needs and the practitioners' services, the potential problem arises of inadequate information being provided by taxpayers or a misunderstanding of clients' needs by practitioners. Another possibility is that clients might even misunderstand what the practitioner can do for them. Most taxpayers in this sample used their practitioners for tax matters only, but around 40% sought business advice or audit services.

Overall, business taxpayers had a reasonable knowledge of tax issues and the penalties associated with noncompliance. About 24% had been penalised for late filing, 35% for late payment, and just over half had been audited at least once.

A number of questions were used to reveal the kind of relationship business taxpayers had with their practitioners. Responses were surprisingly quite evenly divided between assuming the tax practitioner knew the taxpayer's preference, being explicit in stating preferences and leaving it to the practitioner to decide what was best. Most times, taxpayers accepted their practitioners' advice but over half reported having occasion to express disappointment. Taxpayers acknowledged that on occasion they would seek advice elsewhere and discuss alternatives with their practitioner. In other words, business taxpayers were willing and able to question – they did not always acquiesce.

The vast majority of taxpayers indicated that the practitioner was a trusted confidant insofar as they disclosed all of the firms' tax related information to them. Most business taxpayers were familiar with the concept of aggressive advice and agreed that such advice: (a) favoured a taxpayer's tax position on a questionable item (73%), (b) may not be upheld if challenged by a court (68%), (c) goes against the policy intent of tax law but is still within the letter of the law (68%), (d) had a higher chance of failure than success if challenged by IRD (65%), (e) involves contrived arrangements (60%), and (f) involves noncommercial arrangements (54%).

The last part of the chapter described the development and construction of measures of the core concepts for hypotheses testing – the expectation-experience gap, satisfaction with and retention of practitioners, trust in practitioners, agreement with practitioners' advice, expectation of aggressive advice, personal and business tax ethics, personal risk propensity, and perceptions of sanction risk.

While describing and demonstrating the psychometric soundness of these measures, mean scores, standard deviations and percentages in agreement have also been reported to round out the picture of the profile of business taxpayers involved in this study.

The expectation-experience gap was measured in terms of three dimensions – technically proficient, aggressive advice and cautious advice. Most importantly, taxpayers expected their practitioners to be technically proficient (that is, help to file an accurate return, minimise tax, avoid serious penalties, explain tax law and regulations clearly, know many ways to save taxes, reduce uncertainties, keep up to date with changes, save time, and mention risks). This is followed by cautious advice (that is, not to take deductions that fall within any grey areas of tax law and assist firm to make legitimate claims). Third most important on average for this group was the expectation that their practitioners would provide aggressive advice (that is, help to exploit tax loopholes, be creative in dealing with tax matters, provide aggressive advice where tax law is ambiguous and promote tax effective schemes).

These technically proficient and cautious advice expectations are generally consistent with the literature on the reasons taxpayers engage tax practitioners. However, aggressive advice expectations appeared inconsistent with findings from numerous studies, which indicated that taxpayers preferred conservative advice (Hite & McGill, 1992; Tan, 1999). It needs to be noted that this is the first study in which a multi-item scale has been used for the expectation construct, thereby providing a more reliable and valid measure. It is important to emphasise also that in this study taxpayers were encouraged to express their 'cautious' side and their 'aggressive' side. One did not exclude the other.

Taxpayers play their role with many "faces" (Goffman 1971) and in partnership with a trusted practitioner, the "face" of caution may change to one of aggression. Taxpayers clearly agreed on wanting practitioner proficiency. However, it appeared that some taxpayers wanted more aggressive advice than others, particularly when the law was not clear-cut. Also, some wanted more cautious advice than others in that they did not want to get into trouble with the law. It is interesting that the 3 expectation dimensions were positively and not negatively correlated. The results imply that taxpayers are saying, "Yes, keep me safe; yes, be aggressive; and yes, save me money!" There is a lack of simplicity in how taxpayers think about what their practitioners can deliver. If these conflicting expectations are simultaneously sent to practitioners, practitioners are bound to experience role ambiguity and role conflict. It will be interesting to see whether tax practitioners experienced role ambiguity and role conflict and if so, how they cope with it. Chapter 8 explores this area in further depth.

For the three scales discussed above, the gap was in the expected direction – expectations were generally higher than the experience of the service offered. Whether these apparent differences in perception are statistically significant will be tested in the next chapter.

In spite of their differences, satisfaction with practitioners was high (86% were happy with services and 90% wished to retain their practitioners). Trust in practitioners was also high (with 96% falling above the midpoint of the trust scale) suggesting that most respondents had a good relationship with their practitioners. An interesting question that can be raised here is what helps to establish a good relationship between the practitioner and client? If experience falls short of expectations, will this have an adverse effect on the relationship? These relationships will also be explored further in the next chapter.

Since taxpayers wanted to stay safe and also to save tax, it was interesting to find out how they would respond to aggressive advice from their practitioners. Two hypothetical scenarios were used to test whether these business taxpayers would actually accept aggressive advice from their practitioners if given in a situation where the law was ambiguous. It is interesting that more than half (about 62%) agreed that they would accept it. It appears that business taxpayers will be led if their practitioners advise them to allow this. Supporting this idea that a substantial proportion (although not all) of business taxpayers rely heavily on their practitioners are the data on business ethics, risk propensity and perceived sanction risk.

The measures of personal tax ethics and business tax ethics were interesting in suggesting that respondents considered themselves as being more ethical than other business taxpayers. There is a possibility of a social desirability bias exacerbated by the use of a one-item scale, but it is more likely that taxpayers really believe this about themselves. Taxpayers have many coping mechanisms for convincing themselves that they are honest and good people, even if the data prove otherwise (Braithwaite 2009).

As the respondents presented themselves as being more cautious and law abiding than other business taxpayers, it is not surprising that they considered it highly likely that other business taxpayers would ask their accountants to take illegitimate measures to minimise tax. However, they were of the view that neither others' practitioners nor their own would oblige. Based on this feedback, it appears that business taxpayers have high regard for the professionalism of practitioners. It is interesting that the majority of the firms used by the respondents were Chartered Accounting firms.

Risk propensity and perceived sanction risk varied among respondents. In general, however, this sample of business taxpayers were not high scorers on risk taking. About 70% of respondents indicated that they needed more than 50% certainty to make an ambiguous expense claim. About 40% of respondents perceived that there was more than a 50% chance that they would be audited and would suffer a severe penalty. When one considers that only 54% reported ever having an audit, out of which only 10% suffered shortfall penalties, the expectation of being audited and severely penalised on the occasion of one specific misdemeanour is somewhat exaggerated.

This chapter discussed the research method and provided background information about the respondents and the concepts. However, the relationships between the concepts have not been considered in further depth. The next chapter describes the testing of a set of eight hypotheses through which the following themes in understanding the client-practitioner relationship, from the taxpayers' perspective, were addressed:

- the role of tax practitioners as perceived and experienced by business taxpayers and the fulfilment of their expectations;
- the contributing factors that helped establish a positive and stable practitioner-client relationship; in particular, the effect of any mismatch between the three dimensions of expectations and experiences, and trust on their relationships; and
- the acceptance of aggressive advice from tax practitioners and what drives their acceptance.

Chapter 6
Taxpayers' Role Relations With Their Practitioners and Agreement With Aggressive Advice

6.1 Introduction

The previous chapter showed that there were three distinct dimensions of expectations which taxpayers hold concerning their practitioners who, they expect, will be technically proficient, and able to offer both aggressive advice and cautious advice. A clear majority of taxpayers expected their practitioners to be technically proficient and cautious. The sample was divided more evenly on aggressive advice. Several hypotheses were developed for this study to provide some insights into how and when these dimensions of expectations helped establish a stable relationship between practitioners and clients, and what factors influenced taxpayers' agreement with aggressive advice. The central idea was that if a practitioner met the role expectations of the client and was considered trustworthy, the relationship would be valued by the taxpayer. Should aggressive tax advice be given, it would be accepted or rejected by the taxpayer depending on the taxpayer's expectation of the practitioner as well as the taxpayer's assessment of risk, personal norms and social norms. The results of the hypotheses testing are reported in this chapter.

The first hypothesis sets out to examine whether or not taxpayers received what they expected from their practitioners; that is, whether or not there is an expectation-experience gap. With expectations reduced to three underlying factors (see Chapter 5), Hypothesis 1 was refined for testing as follows:

> H1 (taxpayers): There will be an expectation/experience gap between taxpayers' expectations and experiences with regard to the proficiency, caution and aggressiveness in the services provided by their practitioners.

With the merging and averaging of the scale for overall satisfaction with services and intention to retain practitioners, Hypotheses 2 and 3 were also restated as follows:

H2 (taxpayers): The expectation-experience gap will have a negative effect on satisfaction.

H3 (taxpayers): Taxpayers' trust in the practitioner will have a positive effect on satisfaction.

The other hypotheses that were tested remained the same as developed in Chapter 4:

H4 (taxpayers): In an ambiguous tax situation, expectations of aggressive advice will be positively associated with taxpayers' agreement with practitioners' aggressive advice.

H5 (taxpayers): In an ambiguous tax situation, personal tax ethics will influence taxpayers' agreement with practitioners' aggressive advice.

H6 (taxpayers): In an ambiguous tax situation, perceived business tax ethics will influence taxpayers' agreement with practitioners' aggressive advice.

H7 (taxpayers) – Taxpayers with a higher risk propensity will agree more with their practitioners' aggressive advice on an ambiguous tax situation than will those with a lower risk propensity.

H8 (taxpayers) – Taxpayers with low sanction risk perceptions (perceived probability of detection and of severe tax penalties) will agree more with their practitioners' aggressive advice on an ambiguous tax situation than will those with high sanction risk perceptions.

The variables developed in Chapter 5 and used to test the eight hypotheses are summarised in Table 6.1 below.

Table 6.1: Summary of hypotheses and variables used

Hypothesis	Variable (No of items)	Item scores
H1	Expectation – Experience = gap -Technically proficient (9) -Aggressive advice (4) -Cautious advice (2)	1 = strongly disagree 5 = strongly agree
H2	Satisfaction (2)	1 = strongly disagree 5 = strongly agree
H3	Trust (4) Agreement with aggressive advice (2)	1 = strongly disagree 5 = strongly agree 1 = definitely no 5 = definitely yes
H4	Expectation of aggressive advice (4)	1 = strongly disagree 5 = strongly agree
H5	Personal tax ethics (1)	1 = definitely no 5 = definitely yes
H6	Perceived business tax ethics (8)	1 = never 4 = frequently
H7	Risk propensity (2)	0 = 0% certainty 10 = 100% certainty
H8	Perceived sanction risk (2)	0 = 0% chance 10 = 100% chance
Control Variable 1: Firm size	Firm size (1)	1 = SMEs 2 = large firms
Control Variable 2: Audit experience	Audit experience (1)	1 = never audited 2 = audited before

6.2 Business taxpayers' role relations with practitioners

6.2.1 Expectation-experience gap

To examine whether or not there is an expectation-experience gap, the difference between the clients' expectations and experiences on the scales "technically proficient", "aggressive advice" and "cautious advice" were computed.[28]

[28] For example, the technically proficient expectation score minus the technically proficient experience score was obtained for each individual to arrive at the gap for technically proficient. The same was done for the other two gaps, aggressive advice and cautious advice.

A paired-samples t-test was conducted and the results showed that there was a statistically significant difference on all three dimensions (see Table 6.2). Therefore, the first hypothesis that there is an expectation/experience gap between clients' expectations and their experiences with the services provided by their practitioners is well supported.

Table 6.2: Means (SDs) and t-tests for business taxpayers' expectation–experience gaps

Factors	Expectation – Experience Gap Mean (SD)	t-value
Technically Proficient	.56 (.54)	16.185***
Aggressive Advice	.51 (.78)	10.162***
Cautious Advice	.23 (.71)	5.188***

*** $p < .001$

These results suggest that practitioners were not as technically proficient as taxpayers expected. It is interesting that, practitioners were perceived as being neither sufficiently aggressive nor sufficiently cautious. Taxpayers, as a group, appeared to be sending out mixed messages to practitioners. Overall, on the basis of their experience, taxpayers perceived that their practitioners could have done better in all dimensions!

Comments received from some respondents converged with these findings. As pointed out by a number of respondents:

- "The practitioner is expected to be creative in dealing with tax matters provided as long as it is not to the extent of testing the tax law and best practice." (RN 198 – from a listed company with a practitioner from one of the Big 4 CA firms).
- "Although practitioners are expected to be able to exploit tax loopholes to the advantage of our firms, it also depends on the "legitimacy of loopholes" and "its general acceptance as a reasonable tax position." (RN 198).
- "Sometimes the practitioner is too keen to follow the letter of the law." (RN 47 – from a very small firm).
- "It feels as though he is actually working for the IRD, not me; does not give any advice regarding tax loopholes etc. keeps his nose clear." (RN 66 – from a small firm).

- “Would have liked him to be more able to find loopholes.” (RN 139 – from a very small firm).
- “I expect him to operate within the law.” (RN 28 – from a medium firm).
- “His job is to keep me on the right side of the law.” (RN 180 – from a very small firm).
- “…has limited knowledge of legitimate claims and tax law – more interested in their own business than assisting our inaccuracy.” (RN 160 – from a very small firm).

It is clear from these responses that taxpayers used a tax practitioner to keep them safe as well as to help them to minimise taxes within the boundaries of the law. Some perceived no tension between using loopholes and being law abiding. A practitioner, on the other hand, might aspire to being cautious in choosing the tax loopholes available for exploitation.

6.2.2 Effect of gap and trust on satisfaction

If there is a significant gap between role expectations and actual experience, will taxpayers feel dissatisfied with practitioners’ services and will they dissociate themselves from the working relationship? If not, why not? It was hypothesised in this study that the gap would adversely affect taxpayers’ working relationships with practitioners while an important aspect of interpersonal relations, that is, trust would positively affect their relationships.

To test this hypothesis, relationships among gaps in technically proficient, aggressive advice and cautious advice, trust, and practitioner satisfaction were examined by using the Pearson product-moment correlation coefficient. As shown in Table 6.3, all expectation-experience gaps showed a significant negative correlation with satisfaction (that is, overall satisfaction and retention). The results showed that the technically proficient gap had a stronger negative relationship with satisfaction ($r = -.509$; $p < .001$) in comparison to the aggressive advice ($r = -.371$; $p < .001$) and cautious advice gaps ($r = -.257$; $p < .001$). Trust was significantly and positively correlated with satisfaction ($r = .560$; $p < .001$).

Table 6.3: Pearson correlations coefficients among expectation-experience gaps, trust, and satisfaction

Variables	1	2	3	4	5
1. Technically proficient gap	-				
2. Aggressive advice gap	.638***	-			
3. Cautious advice gap	.424***	.288***	-		
4. Trust	-.356***	-.201***	-.188**	-	
5. Satisfaction	-.509***	-.371***	-.257***	.560***	-

** p < .01 *** p < .001

Based on the bivariate analyses, the second and third hypotheses that the three dimensions of expectation-experience gaps and trust would be negatively and positively related to satisfaction respectively are supported. Not surprisingly, the findings suggest that the greater the negative gap, the lower the level of satisfaction; the more taxpayers trust their practitioner the higher would be their satisfaction and commitment to the practitioner-client relationship.

The above bivariate analyses indicate whether or not the independent variables are related to satisfaction individually. This analysis does not tell us the predictive power of the variables as a set or their importance relative to each other. To ascertain the best predictor of satisfaction, a multivariate regression analysis was conducted as it allows the examination of the effect of several independent variables on a dependent variable.

The independent variables, that is, trust and the three dimensions of expectation-experience gaps, were entered into an equation predicting taxpayers' satisfaction. The results of the ordinary least squares multiple regression analysis appears in Table 6.4. It is of note that none of the tolerance statistics was below .2; therefore, multicollinearity in the data was not a concern (Field 2005).

Table 6.4: Standard error (SE), standardised beta coefficients (β), adjusted R^2 for an ordinary least squares regression analysis predicting satisfaction

Predictors	SE	β
Technically proficient gap	.090	-.289***
Aggressive advice gap	.058	-.096
Cautious advice gap	.053	-.030
Trust	.065	.409***
Adjusted R^2 = .40		

*** $p < .001$

From the regression analysis in Table 6.4, only the technically proficient gap and trust were significant predictors of satisfaction. Together the variables predicted 40% of the variability in satisfaction. Of the two significant variables, trust was the more important contributor as indicated by beta coefficients (β). This finding varied from the bivariate analysis as neither aggressive advice nor the cautious advice gap contributed significantly to the regression. It appears that gaps between the taxpayer and tax practitioner in the level of caution and aggressiveness in tax advice fade in significance if the taxpayer trusts the practitioner and regards the practitioner as technically proficient. Hypothesis 2 therefore was only partially supported when the relationships between the variables were analysed together.

The fact that an aggressive or cautious advice gap drops out of the equation in Table 6.4 raises the question of whether or not the variables have been dominated by the proficiency and trust variables. Before dismissing their predictive capacity, a reconceptualisation of the problem will allow a further probe of the importance of the gap between expectations and experiences of aggressive or cautious tax advice. This reconceptualisation has two components. First, both an aggressive and a cautious advice gap as shown in Table 6.3 had strong correlations with proficiency. Therefore an analysis which examined these variables without the influence of proficiency would prove interesting. Second, trust was strongly related to satisfaction. If trust and satisfaction were combined, a broader dependent variable could be used, that is, one representing a trusting stable relationship.

To investigate how successfully an aggressive or cautious advice gap (match) could predict a trusting stable relationship, a hierarchical linear regression analysis was carried out in which the aggressive advice and cautious advice gap were entered on the first and second step. A single scale for trusting, stable relationship was obtained by summing the items under trust and satisfaction and dividing by the number of items, that is, 6 ($M = 4.25$; $SD = .547$; *alpha* = .71).

Table 6.5 displays the results. When the aggressive advice gap variable was entered alone, it significantly predicted a negative trusting stable relationship ($F = 16.125$, $p < .001$). The R^2, however, was a relatively low 7% (adjusted R^2 = 6%). When cautious advice was added, it improved the prediction slightly by 7% ($F = 18.388$, $p < .001$). When the two variables were entered together in the regression model, the cautious advice gap was a stronger predictor than the aggressive advice gap. Lastly, when the technically proficient gap was considered together with the other two gap variables, it significantly improved the prediction. The R^2 change was 11% ($F = 25.482$, $p < .001$) and the regression model explained 25% (adjusted R^2 = 24%) of the variance in trusting, stable relationship. The size of the technically proficient gap appears to be the most important factor in predicting a trusting, stable relationship. The qualitative data analysis also converges with the above analyses. For instance, one respondent from a very small firm pointed out, "we have recently changed accountant for the previous one had made many mistakes" (RN 164). The technical competence of the practitioner is certainly of utmost importance to taxpayers' commitment to the working relationship.

Table 6.5: Hierarchical multiple regression analysis summary for technically proficient, aggressive advice, and cautious advice gap, predicting trusting, stable relationship

Variable	B	SE	β	R^2	R^2 change
Step 1					
Aggressive advice gap	-.197	.049	-.257***	.066	.066***
Constant	4.269	.037			
Step 2					
Aggressive advice gap	-.134	.049	-.175**	.139	.073***
Cautious advice gap	-.198	.045	-.283***		
Constant	4.354	.041			
Step 3					
Aggressive advice gap	-.042	.049	-.054	.253	.113***
Cautious advice gap	-.016	.052	-.023		
Technically Proficient gap	-.461	.079	-.462***		
Constant	4.501	.046			

** $p < .01$ *** $p < .001$

6.2.3 Summary of findings on effect of expectation-experience gap, trust and satisfaction

The implications of these findings shift attention from taxpayer preferences for aggressive or cautious advice toward assessment of their tax practitioners' overall competence, knowledge, and willingness to look after their clients' interests. Chapter 5 tells us that a technically proficient practitioner is what most taxpayers primarily aim for. Taxpayers who report an expectation-experience match on proficiency also are inclined to report a match on cautious and aggressive advice expectations and experiences. These cross-sectional data, however, cannot tell us how the three gap variables are interconnected. For instance, does an aggressive advice gap predispose individuals to judge their practitioner as incompetent or does a perception of competence allow taxpayers to bring their expectations for aggressive advice in line with what the practitioner is offering? What can be concluded from these data is that the most important determinant of a trusting, stable relationship is being technically proficient.

The interpretation that perceived proficiency could overrule an aggressive expectation-experience gap, in particular, is plausible when considered against the background information provided in Chapter 5. Although taxpayers perceived a gap in aggressive and cautious advice, their practitioners might have explained to them their tax situation and why the advice provided was not in accordance with what they expected. An understanding of the reasons behind the advice might have built trust and made such gaps less salient in their practitioner satisfaction/retention decision. Practitioners, as indicated in the literature, can exert influence over taxpayers' tax reporting decisions. Taxpayers, on the other hand, may also influence their practitioners regarding the type of advice they prefer. The interactions and communication between them create opportunities for each to influence the other's decisions.

Taxpayers' comments were also useful for reinforcing the point that these taxpayers routinely discussed their "situations", the "options", the "grey areas", and the "risk, case by case" with their practitioners. These views are supported by the quantitative responses shown in Table 5.4 (in Chapter 5) where a majority indicated that they discussed alternative measures with practitioners. These insights suggest that the partnership between the practitioner and client has an important influence on the latter's evaluation of the type of advice provided by practitioners. As indicated by Sakurai and Braithwaite (2001), it is a team play between taxpayers and practitioners to a considerable degree when tax decisions are made, and this view is also supported by the comments received from taxpayers as discussed in the previous chapter (see Section 5.8).

To have such an open relationship, it is of utmost importance that taxpayers are able to trust their practitioners. As the findings of this study show, trust in practitioner emerged as an important interpersonal factor in the quantitative as well as the qualitative analyses (see Section 5.9.4). Trust certainly helps to build a good relationship between taxpayers and practitioners.

These findings perhaps explained why prior studies (for example, Hite et al. 1992; Murphy 2001; Tan 1999) found that taxpayers wished to retain their practitioners even if they disagreed with particular advice on treatment of items where tax law was ambiguous. Most taxpayers do not make such decisions based on one criterion or based on the outcome of one expectation not met. For instance, even though fees charged by tax practitioners were a concern expressed by a number of taxpayers in this study, the majority were still willing to retain their services. They would change their practitioners only if they could be assured that they would be better off with another practitioner. Within this context, it is interesting to draw on the findings in Chapter 5 showing that this sample of business taxpayers considered that others would be pushing for more aggressive advice, but their views that the practitioners would not oblige were fairly uniform.

In summary, trust in, satisfaction with, and retention of, a tax practitioner among business taxpayers seems to be driven predominantly by the perception that the tax practitioner matches their expectations of technical proficiency. Meeting expectations on cautious or aggressive advice matters to some extent, but both fade in importance against the proficiency gap.

To provide further insights into the role relationships of taxpayers and practitioners, this study explored one hypothetical role episode in which taxpayers were asked to respond to the aggressive advice provided by their practitioner. This is a pertinent area to investigate as practitioners, when presented by their clients with ambiguous tax issues, may resolve the issue in quite different ways (Carnes et al. 1996a). One of the ways is to exploit the tax law to their clients' advantage. The next section therefore examines the taxpayers' agreement with practitioners' aggressive advice and the factors that may impact on their decisions. Whether the expectation-experience gaps and the trusting, stable relationship discussed earlier have any part to play in taxpayers' agreement with aggressive advice are also explored by conducting a hierarchical regression analysis.

6.3 Business taxpayers' agreement with practitioners' aggressive advice

6.3.1 Factors associated with agreement with aggressive advice

The correlation matrix between the independent variables of interest and the dependent variable is shown in Table 6.6. The results were initially checked for multicollinearity, which indicated that there was no problem. None of the tolerance statistics was below .2 indicating that collinearity was not likely to be a problem (Field 2005).

Preliminary results showed that there were significant relationships between five variables and agreement with aggressive advice. A trusting, stable relationship (r = .138; $p < .05$), risk propensity (r = -.229; $p < .001$) and aggressive expectation (r = .142; $p < .05$) were directly related to agreement with aggressive advice. The cautious advice gap (r = -.138; $p < .05$), and perception of sanction risk (r = -.290; $p < .001$), on the other hand, were negatively related to agreement with aggressive advice. That is, both taxpayers who had established a positive trusting, stable relationship with their practitioner, and those with higher risk propensity and expectation of aggressive advice were more agreeable to accepting aggressive advice. In contrast, taxpayers with a higher cautious advice gap and higher perception of sanction risk were less agreeable to aggressive advice.

An hierarchical multiple regression analysis with agreement with aggressive advice as the dependent variable was used to explore the relative importance of the predictor variables. Variables were entered into the equation in three steps. First, size of business and audit experience were entered into the equation as control variables because it was postulated that these background characteristics could influence a taxpayer's general approach to aggressive advice. Results displayed in Table 6.7 show that these two control variables accounted for only .5% of the variance in agreement with aggressive advice and there was no significant differences (F = .480, $p > .05$). At the level of individual variables, neither size nor audit experience had any significant impact on agreement with aggressive advice in this New Zealand sample.