

Abstract

This study investigated how personal ethics and social norms interact with deterrence in their effects on tax compliance. In line with earlier research, it is argued and shown that strong personal tax ethics reduce effects of deterrence. Strong tax ethics basically exclude tax evasion from one's behavioural options and no deterrence is required to maintain tax honesty. Such personal ethics are partly based on social norms that are internalised in one's own ethical make-up. In contrast, social norms that are not internalised (for example, because one does not identify with the group holding these norms) can enhance effects of deterrence, because they add social costs to the material costs of sanctions, such as reputation threat and stigma.

The study was based on data from *The Community Hopes, Fears, and Actions Survey* (Braithwaite, 2001) involving 2040 Australian participants. It investigated three different self-reported acts of tax evasion, namely pay income underreporting, non-pay income underreporting and exaggerations of deductions; and three aspects of deterrence incorporating legal sanctions, namely the perceived probability of detection, the perceived probability of legal consequences and the perceived severity of the consequences. Although the importance of the three deterrence aspects varied somewhat between the three forms of evasion, perceived sanction severity was overall the most relevant aspect. The results showed that personal taxpaying ethics were negatively related to tax evasion, while social norms (beyond those internalised as personal ethics) had no direct effect. Personal ethics moderated the deterring effects of legal sanctions; deterrence was stronger when people's ethics were only weakly opposed to tax evasion. Social norms moderated the effects of deterrence when personal norms were controlled and identification as Australians was weak: the deterring effects of legal sanctions were greater when social norms were strongly opposed to tax cheating.

The study thus provides a strong argument for the investment of much regulatory effort in the establishment of supportive taxpaying norms and culture. In line with the compliance model of the Australian Taxation Office, it would be important to nurture personal norms of tax honesty, because this would make any more costly and potentially alienating regulatory activities unnecessary. However, when personal norms fail and regulatory measures would escalate to more stringent levels of enforcement, the effects of deterrence would be greatly supported by a positive tax paying culture; again the nurture of supportive norms is paramount. Finally, by building strong identification with one's community and representative institutions as well as furthering positive taxpaying norms, tax regulators would move taxpayers down to the cooperative base of the compliance model's regulatory pyramid.