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# Measuring the tax gap of business taxpayers in Australia

## **Abstract**

The 'tax gap' is the difference between the tax that would have been determined if all taxpayers had reported all of their activities and transactions correctly, and the tax determined in practice. Generally, tax gap estimates exclude illegal sources of income. This article considers how best to estimate the tax gap attributable to business taxpayers in Australia.

## **Keywords**

tax gap, ATO, business taxpayers, tax collection

## MEASURING THE TAX GAP OF BUSINESS TAXPAYERS IN AUSTRALIA

SYLVIA VILLIOS\*

The 'tax gap' is the difference between the tax that would have been determined if all taxpayers had reported all of their activities and transactions correctly, and the tax determined in practice. Generally, tax gap estimates exclude illegal sources of income. This article considers how best to estimate the tax gap attributable to business taxpayers in Australia.

In Australia, the government does not attempt to estimate the total tax gap but instead undertakes vigorous risk assessments to identify and address areas where this gap may be or potentially become significant.<sup>1</sup> For example, in relation to the Goods and Services Tax (GST) gap risk, the Australian Taxation Office (ATO) develops indicators using Australian Bureau of Statistics (ABS) data, including GST growth in relation to ABS household expenditure data, GST growth by surveys of enterprise, GST trends by industry and indicators of ATO efficacy in relation to GST fraud.<sup>2</sup>

This approach has been criticised by the Australian National Audit Office and the Joint Committee of Public Accountants and Audit (JCPAA). In particular, JCPAA have commented that the ATO should establish and maintain a dynamic mechanism to determine an estimate of the tax gap using appropriate ABS economy-wide business indicators.<sup>3</sup>

Tax gap estimation is beneficial and important as it is a means of identifying the types and level of non-compliance that contribute to the tax gap. It can provide improved efficiency of resource allocation within a revenue authority to combat non-compliance and can also act as a measure of effectiveness of a revenue authority.

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<sup>1</sup> Jacqui McManus and Neil Warren, 'The Case for Measuring Tax Gap' (2006) 4(1) *eJournal of Tax Research* [70] <<http://www.austlii.edu.au/au/journals/eJTR/2006/3.html#fn1>> at 1 February 2012.

<sup>2</sup> *Ibid* [70].

<sup>3</sup> *Ibid* [71].

## BACKGROUND

A tax gap may arise either because of assessment risk or collection risk. Assessment risk is the difference between tax that is due and tax actually assessed by the tax authorities as owing by the taxpayer. This includes the gap attributable to taxpayers underreporting their income and not lodging their tax returns. The major portion of the tax gap is caused by assessment risk (around 90% of the overall tax gap in developed economies).<sup>4</sup>

Collection risk is the difference between tax payments received and tax actually assessed by the taxpayer. In the US, this difference is largely caused by accidental non-compliance and employers' failure to withhold income and employment taxes.<sup>5</sup>

## METHODS OF TAX GAP ESTIMATION

Attempts to quantify the tax gap can be divided into macro and micro methods. Macro methods rely on macro indicator variables like monetary and physical input demand, or on information from national and financial accounts, to determine the overall size of the tax gap.

Conversely, micro methods rely on data retrieved from individual taxpayers in the form of surveys and tax audits. Such methods use a bottom-up approach to derive estimates of the size of the tax gap in the economy as a whole.

### Macro Approaches to Tax Gap Estimation

#### *The Currency Demand Methods*

The currency demand method is based on the concept that dishonest taxpayers largely transact in cash in order to avoid leaving detectable traces. This model suggests the degree to which activities are shifted into the unofficial sector could be determined by the level of taxation, the complexity of the tax system, GDP per capita and the interest rate on savings deposits. Accordingly, this model is based on calculating the 'excess' demand for currency to estimate the size of the tax gap and explaining this by reference to these indicators.<sup>6</sup>

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<sup>4</sup> US Department of the Treasury, *A Comprehensive Strategy for Reducing the Tax Gap* (2006) <[http://www.irs.gov/pub/irs-news/comprehensive\\_strategy.pdf](http://www.irs.gov/pub/irs-news/comprehensive_strategy.pdf)> at 1 February 2012.

<sup>5</sup> *Ibid.*

<sup>6</sup> Philip Cagan, 'The Demand for Currency Relative to the Total Money Supply' (1958) 66(3) *Journal of Political Economy* 302-328; Peter Gutman, 'The Subterranean Economy' (1977) 34(1) *Financial Analyst Journal* 24-27.

### ***Physical Input Methods***

The physical input method is based on the premise that electric power consumption is an appropriate indicator for overall economic activity. For example, electricity consumption has been used (as a proxy for the overall economy) minus estimated official GDP to estimate the tax gap.<sup>7</sup>

### ***Macro Accounting Methods***

Macro accounting approaches identify tax gaps by comparing data from national and financial accounts of countries. The underlying concept is that discrepancies in these accounts can be reconciled to estimate a country's tax gap.

### **Micro Approaches to Tax Gap Estimation**

#### ***Survey Methods***

In developed economies, tax authorities also rely on survey methods to determine the size of the tax gap. A questionnaire survey can be in the form of telephone interviews, face-to-face interviews or postal questionnaires. For example, the Swedish tax authority sends out questionnaires to corporations and individuals regarding their activities and transactions, and undertakes surveys of particular sectors and occurrences.<sup>8</sup>

#### ***Tax Audit Methods***

Tax audit methods involve observing persons and firms through careful audits of information supplied by taxpayers to the tax authorities. Audits about taxpayers' own information regarding income and deductions can to some extent reveal the accuracy of such information. Provided the sampling process is random, it is straightforward to extrapolate the information retrieved in the tax audits to the whole taxpayer population.<sup>9</sup>

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<sup>7</sup> Daniel Kaufmann and Aleksander Kaliberda, 'Integrating the Unofficial Economy into the Dynamics of Post Socialist Economies: A Framework of Analyses and Evidence' in Bartłomiej Kamiński (ed), *Economic Transition in Russia and the New States of Eurasia* (1996) 117.

<sup>8</sup> Swedish National Tax Agency, *Tax Gap Map for Sweden – How was it created and how can it be used?* (2008) <[http://www.skatteverket.se/download/18.5cbdbba811c9a768f0c80005186/Report\\_2008\\_1B.pdf](http://www.skatteverket.se/download/18.5cbdbba811c9a768f0c80005186/Report_2008_1B.pdf)> at 1 February 2011.

<sup>9</sup> Clemens Fuest and Nadine Riedel, *Tax evasion, tax avoidance and tax expenditures in developing countries: A review of the literature* (2009) <<http://www.sbs.ox.ac.uk/centres/tax/Documents/reports/TaxEvasionReportDFIDFINAL1906.pdf>> at 14 February 2011.

One example of the use of the tax audit method is the National Research Program (NRP) conducted in the US in 2001, where the US government established a program to measure taxpayer compliance.<sup>10</sup> NRP is based on a large sample of 46,000 tax returns that were randomly selected for review and examination. Using sample weights according to taxpayer characteristics, the information gained from the audits, and the non-compliance behaviour of the randomly selected taxpayer, a sample was extrapolated to the rest of the population and aggregated to measure the tax gap.

### Best Method to Use

Each of the methods described above has various strengths and inherent weaknesses.

Currency demand methods have been heavily criticised by the Organisation for Economic Cooperation and Development (OECD) that has commented such models are 'unsuitable for estimating the underground economy primarily because they are based on modelling assumptions that cannot be justified...'.<sup>11</sup>

The Physical Input method has been criticised, as not all shadow economy activities require a considerable amount of electricity. Technical progress has made electricity more efficient, rendering tax gap estimates inaccurate.<sup>12</sup>

Macro accounting methods can also produce inaccurate results given they are calculated based on national data that may be inaccurate for statistical reasons or insufficient data quality.<sup>13</sup>

Importantly, all of the macro methods discussed above have the disadvantage that they produce aggregate information on the tax gap only. A major advantage of micro methods is that the tax gap can be separated according to taxpayer groups and type of income tax being evaded. Accordingly, a study that measures the tax gap attributable to Australian business taxpayers should preferably adopt a micro method of measurement, either by survey or audit.

The disadvantages of survey methods are that they are costly and time consuming. Further, the accuracy of the data is dependent upon the willingness of respondents to answer questions truthfully. More specifically, the sensitivity of the topics of tax avoidance and evasion casts doubt upon the respondents' veracity. Studies show that

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<sup>10</sup> Internal Revenue Service, *IRS Updates Tax Gap Estimates* (2006) <<http://www.irs.gov/newsroom/article/0,,id=154496,00.html>> at 1 February 2011.

<sup>11</sup> Organisation for Economic Co-operation and Development, *Measuring the Non-Observed Economy – A Handbook* (2002) 190.

<sup>12</sup> Clemens Fuest and Nadine Riedel, *Tax evasion, tax avoidance and tax expenditures in developing countries: A review of the literature* (2009) <<http://www.sbs.ox.ac.uk/centres/tax/Documents/reports/TaxEvasionReportDFIDFINAL1906.pdf>> at 14 February 2011.

<sup>13</sup> Above n 8.

the results of tax gap estimate surveys are perceived to be very sensitive to the way the questionnaire is formulated.<sup>14</sup>

Generally, micro approaches based on information from random tax audits are most likely to deliver reliable tax gap estimates.<sup>15</sup> However, in the small business context, where cash transactions are commonplace, opportunities for evasion are high and resources are often scarce for field auditing.<sup>16</sup> Even when high investments are made in auditing, uncovering 'hidden cash' is never an easy task without an adequate audit trail.<sup>17</sup> Given the small business sector comprises a large portion of the overall Australian business population, audit methods are unlikely to be useful. Accordingly, it appears a survey method is the better method to use for such research. This is especially so if the questionnaire is formulated so that it does not suffer from problems related to subjectivity in the answers.

If a survey method is adopted to measure the tax gap attributable to Australian business taxpayers, the next steps will involve considering sample selection and then developing a survey instrument.

## **SURVEY METHOD**

### **Sample Selection**

The population of interest is Australian business taxpayers. The sampling frame for this survey should come from the ABS business register. Using the ABS register means the accuracy of the study will be reliant on the register being reliable and comprehensive. This may be problematic in the event that there are high turnover rates of businesses or if businesses deliberately fail to register totally or in part.

The ABS categorises Australian businesses by employment size ranges, industry, main state of operation, institutional sector, type of legal structure and annual turnover size ranges. For the purpose of this study, the best estimation of the tax gap

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<sup>14</sup> Gunnar Mogensen et al., *The Shadow Economy in Denmark 1994: Measurement and Results* (1995); Friedrich Schneider, 'Shadow Economies and Corruption all over the World: new estimates for 145 countries' (2007) 1(9) *Economics eJournal* <<http://www.economics-ejournal.org/economics/journalarticles/2007-9>> at 1 February 2011.

<sup>15</sup> IRS Economic Analysis and Modelling Group, Brian Erard and Jonathan Feinstein, *Estimating the Federal Income Tax Gap Using Operational Audit Data* (2001).

<sup>16</sup> David Joulfaian and Mark Rider, 'Differential Taxation and Tax Evasion by Small Business' (1998) 51 *National Tax Journal* 675-687.

<sup>17</sup> Cash Economy Task Force, *Improving Tax Compliance in The Cash Economy* (1998) <<http://ctsi.anu.edu.au/publications/ATOPubs/improving%20tax%20compliance.pdf>> at 1 February 2011; M Dornstein, 'Compliance with legal and bureaucratic rules: The case of self-employed taxpayers in Israel' (1976) 29 *Human Relations* 1019-1034.

can be made if Australian businesses are categorised by size. This is the most appropriate category as 96% of businesses in the Australian private sector are 'small businesses' (0 - 20 employees),<sup>18</sup> and small business taxpayers perceive the tax system differently to other business taxpayers.<sup>19</sup>

For the tax gap estimation to be as accurate as possible, all categories of business taxpayers (small, medium and large businesses) should be included in the sample. The sample selection should be representative of each category as a proportion of all categories of Australian business taxpayers. Therefore, the most appropriate sample selection method is the probability proportional to size (PPS) sampling method. This method will give more highly represented categories on the register a greater chance of selection than less represented ones. Specifically, the probability of selecting the category will be directly proportional to its size. For example, in this study, 96% of the sample selected will be small business taxpayers. In order to select a PPS sample, each category of business in the framework must have an associated 'measure of size' which is usually based on the total population. There were 2,132,412 actively trading businesses in Australia as at June 2011.<sup>20</sup> This is the size measure that will provide the basis for selecting some categories of business with greater probability than others.

Once selection ranges are determined for the categories, a sample can be selected through a simple random selection so the information retrieved in the survey can be extrapolated to the entire Australian business taxpayer population. Given the large number of Australian businesses in each category on the register, it is unlikely the same business will be selected more than once, therefore rendering systematic selection unnecessary.<sup>21</sup>

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<sup>18</sup> Ibid.

<sup>19</sup> Australian Taxation Office, Danger Research Group, *Small business attitudes to tax compliance: A pilot research study for the ATO* (1996); C Coleman and L Freeman, 'The Development of Strategic Marketing Options Directed at Improving Compliance Levels in Small Business' (1994) 11 *Australian Tax Forum* 347-367; C Coleman and L Freeman, 'Cultural Foundations of Taxpayer Attitudes to Voluntary Compliance' (1997) 13 *Australian Tax Forum* 311-336; Margaret McKerchar, 'Understanding Small Business Taxpayers: Their Sources of Information and Level of Knowledge of Taxation' *Australian Tax Forum* 12 (1995) 25-41.

<sup>20</sup> Australian Bureau of Statistics, 'Counts of Australian Businesses, including Entries and Exits: Jun 2007 to Jun 2011' (2012) <<http://www.abs.gov.au/ausstats/abs@.nsf/mf/8165.0>> at 1 February 2011.

<sup>21</sup> P Marsden and J Wright, *Handbook of Survey Research* (2010).

## The Survey Instrument

Numerous statistical models have been developed to estimate 'tax gap'. Much of the research in developing these statistical models has been to identify risk areas that are the sources of tax gap.<sup>22</sup>

The detailed knowledge the tax administrator usually generates regarding risk areas is essentially the source of the tax gap.

In developing the survey, the various risk areas regarding Australian business taxpayers have been considered, based on both Australian and international experiences.<sup>23</sup> It is intended that an advanced statistical model can be then be applied to the survey responses, to extrapolate an estimate of the tax gap for business taxpayers in Australia.<sup>24</sup>

Section A considers the business taxpayers' perception of government institutions and the ATO. Question 1 has been formulated around the proposition that firms operate in the underground economy (and consequently add to the tax gap) due to weaknesses in political and social institutions, like bureaucracy, over-regulation, corruption and a weak legal system.<sup>25</sup>

Question 2 is based on two Australian studies that have explored small business taxpayers' perceptions of the tax office and the tax system.<sup>26</sup> The willingness of small business taxpayers to establish a cooperative relationship with the ATO has not always been reciprocated in the past.<sup>27</sup> Complaints of tax office inaccessibility have been widespread.<sup>28</sup> Further studies report small business taxpayers as envisaging an

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<sup>22</sup> Fredrich Schneider, 'Shadow Economies of 145 countries all over the world: What do we really know?' (2007) 1(9) *Economics eJournal* <<http://www.economics-ejournal.org/economics/discussionpapers/2007-9>> at 1 February 2011.

<sup>23</sup> See Appendix 1.

<sup>24</sup> See above n 21.

<sup>25</sup> S Johnson et al., 'Why Do Firms Hide? Bribes and Unofficial Activity after Communism' (2000) 76 *Journal of Public Economics* 495-520; Axel Dreher and Freidrich Schneider, *Corruption and the Shadow Economy – An Empirical Analysis* (Working Paper 06-91, Centre for Research in Economics, Management and the Arts, 2006); Eric Friedman, 'Dodging the Grabbing Hand: The Determinants of Unofficial Activity in 69 Countries' (2001) 76(3) *Journal of Public Economics* 459-493.

<sup>26</sup> C Coleman and L Freeman, 'The Development of Strategic Marketing Options Directed at Improving Compliance Levels in Small Business' (1994) 11 *Australian Tax Forum* 347-367; I Wallschutzky and B Gibson, 'Small Business Cost of Tax Compliance' (1993) 10 *Australian Tax Forum* 511-543.

<sup>27</sup> Ibid.

<sup>28</sup> Ibid.

adversarial relationship with tax authorities and wanting to 'win' against 'the taxman'.<sup>29</sup>

Section B considers the business taxpayer's tax morale, that is, their intrinsic willingness to pay taxes. Studies indicate a relationship between low tax morale on the size of the shadow economy,<sup>30</sup> suggesting the tax morale variable can explain up to one-third of the variation in the shadow economy.

A further study identifies five characteristics that increase a taxpayer's morale including political inclusion, accountability and transparency, perceived fairness, effectiveness and the political commitment to shared prosperity.<sup>31</sup> Question 3 is based on each of the five characteristics referred to in the study above.

Section C considers a business taxpayer's attitude towards Australia's economic growth. This section is based on studies which show that for a given tax system, economic growth results in higher tax revenues. This revenue finances a more capable public administration and better public goods, and may give rise to a cycle of development and state building.<sup>32</sup> There are a number of determinants of economic growth that have been identified in the literature, including population growth, the average nutrition of the population, credible protection of property rights and democratic institutions.<sup>33</sup> Question 4 considers the business taxpayer's attitude toward each of the determinants of economic growth, with the exception of Australia's democracy and democratic institutions measured in Section A.

Section D considers the business taxpayer's tendency to act dishonestly. Questions 5, 6 and 7 are based upon a study which found that a lack of morals in a taxpayer is a significant cause of the shadow economy.<sup>34</sup>

Section E considers a business taxpayer's attitude toward ATO efficiency. Studies show the size of a country's tax gap depends on the scope and efficiency of the national tax administration. Generally, studies for developed economies have shown

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<sup>29</sup> Australian Taxation Office, Danger Research Group, *Small business attitudes to tax compliance: A pilot research study for the ATO* (1996).

<sup>30</sup> C Coleman and L Freeman, 'Cultural Foundations of Taxpayer Attitudes to Voluntary Compliance' (1997) 13 *Australian Tax Forum* 311–336; Benno Torgler and Freidrich Schneider, 'The Impact of Tax Morale and Institutional Quality on the Shadow Economy' (2009) 30 *Journal of Economic Psychology* 228–245.

<sup>31</sup> M Everest-Phillips, 'Business Tax as State Building in Developing Countries: Applying Governance Principles in Private Sector Development' (2008) 8 *International Journal of Regulation and Governance* 123–154.

<sup>32</sup> *Ibid.*

<sup>33</sup> *Ibid.*

<sup>34</sup> Bruno Frey and Hannelore Weck-Hanneman, 'The hidden economy as an 'unobserved' variable' (1984) 26(1) *European Economic Review* 33–53.

a positive relationship between tax auditing effort and taxpayer compliance.<sup>35</sup> Further, the risk of detection likely also plays a part in the extent of the shadow economy or tax evasion.<sup>36</sup> Questions 10 and 11 consider Australian business taxpayers' attitudes toward ATO presence. They also consider whether these taxpayers are concerned about the likelihood of being caught for tax evasion and the consequences.

Section F considers the behaviour of Australian business taxpayers that transact in cash. Studies indicate that by far the most important determinant of tax compliance is income source and that individuals fail to declare business income received in cash, at a rate of approximately 50%. The strong relationship between tax evasion and income source suggests the primary causal factor of evasion is opportunity.<sup>37</sup>

Questions 10 and 11 gauge how much of the business taxpayer's total revenue is collected in cash, both as a percentage and dollar value. Question 12 considers how much of the business taxpayer's total business income was declared to the ATO.

Question 13 further considers how much opportunity the business taxpayer has to illegally reduce their tax liability through cash transactions, whereas Question 14 investigates the business taxpayer's opinion as to which types of business taxpayers have the best opportunity to reduce tax illegally through cash transactions. In this context business taxpayers are divided into the ABS statistical categories that have been modified in the sample selection process.

Section G examines the business taxpayer's knowledge of tax law. In the Australian context, studies have found that small business taxpayers do not have adequate knowledge of tax law to meet their obligations.<sup>38</sup>

In Australia, a high proportion of taxpayers (75%), including wage and salary earners, rely on a tax adviser or tax agent to complete their yearly tax returns.<sup>39</sup> In most cases, the reason given for seeking such assistance is to fulfil tax obligations

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<sup>35</sup> J Slemrod, M Blumenthal and C Christian, 'Tax Payer Response to an Increased Probability of Audit: Evidence from a Controlled Experiment in Minnesota' (2001) 79(3) *Journal of Public Economics* 455-483.

<sup>36</sup> *Ibid.*

<sup>37</sup> Susan Morse, Stewart Karlinsky and Joseph Bankman, 'Cash Businesses and Tax Evasion' (2009) 20(1) *Stamford Law & Policy Review* 39.

<sup>38</sup> M McKerchar, 'Understanding Small Business Taxpayers: Their Sources of Information and Level of Knowledge of Taxation' (1995) 12 *Australian Tax Forum* 25-41.

<sup>39</sup> Australian Taxation Office, '2002-2003 Compliance Program' (2003) <<http://www.ato.gov.au/corporate/PrintFriendly.aspx?ms=corporate&doc=/content/39007.htm>> at 1 February 2011.

honestly and without fuss.<sup>40</sup> Questions 14 and 15 concern how much information a taxpayer receives, from which sources, and the quality of that information. Question 16 considers whether in the taxpayer's opinion, they have enough knowledge to comply with their tax obligations. Questions 17 and 18 consider whether the taxpayer relies on a tax advisor in preparing their tax return and their reason for doing so.

Section H considers the Australian business taxpayer's attitude towards other determinants of the tax gap including, high tax burden, high costs of compliance, size of penalty and behaviour of peers.

This question is based on studies that demonstrate increases in the effective tax rate enhance a firm's incentive to operate in the underground economy.<sup>41</sup> It is not a significant part of the survey as there are other studies that fail to establish a significant and negative effect of taxes on the size of the shadow economy.<sup>42</sup>

Further, industry groups and researchers point to the high costs of compliance for small business taxpayers as a reason why concealing income and over-stating deductions is generally accepted as being greater among small business owners.<sup>43</sup>

Tax evasion and shadow market activities are also affected by the size of fines.<sup>44</sup>

A substantial body of research shows that taxpayers who believe their peers evade tax are more likely to evade tax themselves.<sup>45</sup>

Section I concerns the business taxpayer's business and personal demographics and Question 21 determines the category of business taxpayer. This may become

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<sup>40</sup> Yuka Sakurai and Valerie Braithwaite, 'Taxpayers' perceptions of the ideal tax adviser: Playing safe or saving dollars?' (Working Paper No 5, Centre for Tax System Integrity, The Australian National University, 2001).

<sup>41</sup> Friedrich Schneider, 'Shadow Economies and Corruption all over the World: new estimates for 145 countries' (2007) 1(9) *Economics eJournal* <<http://www.economics-ejournal.org/economics/journalarticles/2007-9>> at 1 February 2011.

<sup>42</sup> Eric Friedman, 'Dodging the Grabbing Hand: The Determinants of Unofficial Activity in 69 Countries' (2001) 76(3) *Journal of Public Economics* 459 - 493.

<sup>43</sup> P Noble, 'Qualitative Research Results: The New Zealand Cash Economy - A Study of Tax Evasion amongst Small and Medium Businesses' (Paper presented at the Centre for Tax System Integrity Conference, Australian National University, 4-5 Decemeber 2000); David Joulfaian and Mark Rider, 'Differential Taxation and Tax Evasion by Small Business' (1998) 51 *National Tax Journal* 675 - 687.

<sup>44</sup> Fredrich Schneider, 'The Shadow Economy in Germany: A Blessing or a Curse for the Official Economy?' (2008) 38(1) *Economic Analysis & Policy* 30.

<sup>45</sup> Susan Morse, Stewart Karlinsky and Joseph Bankman, 'Cash Businesses and Tax Evasion' (2009) 20(1) *Stanford Law & Policy Review* 40.

important if the study goes further to quantify the tax gap attributable to each category of business taxpayer.

Question 22 ascertains the gender, age, education level, income level and income source of the survey participant. This question is based on behavioural compliance literature which indicates that these factors may affect tax compliance.<sup>46</sup>

## CONCLUSION

Currently, the Australian government undertakes rigorous risk assessments to identify and address areas where the tax gap may be significant or have the potential to become significant.<sup>47</sup> It appears the next step is to use that information, coupled with further research, to measure Australia's tax gap. Further, this research can be focused on various sectors and groups in the Australian economy. For example, this paper has considered a methodology that could be implemented to measure the tax gap attributable to Australian business taxpayers. By using such information, advancements can be made and ultimately, utilised to further enhance integrity in the Australian tax system.

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<sup>46</sup> Ibid 39.

<sup>47</sup> Above n 1.

## APPENDIX 1

### Australian Business Taxpayers – Tax Gap Study

#### Scope of the Survey

The tax gap is the difference between the tax that would have been determined if all taxpayers had reported all of their activities and transactions correctly, and the tax determined in practice.

**AS AN AUSTRALIAN BUSINESS TAXPAYER, YOU HAVE BEEN CHOSEN AT RANDOM TO TAKE PART IN THIS SURVEY.** If you are not an Australian business taxpayer, please return the blank survey form to Atax in the reply paid envelope provided.

#### Confidentiality

All responses received will be treated as strictly confidential and the ATO will not have access to individual replies. Please note that all responses are anonymous. In any case, the confidentiality of your reply will be preserved with only statistical summaries of the survey data being made available to the ATO.

#### Completing the Questionnaire

You can answer most questions by ticking the appropriate boxes provided. You will be able to answer all the questions without needing to consult your tax adviser. Answering the survey should take about 15 to 20 minutes. Please return your completed survey form to Atax in the reply paid envelopes provided.

Responses to this survey are confidential. Please do not include your name on this survey.

### SECTION A PERCEPTION OF OUR INSTITUTIONS OF GOVERNMENT AND THE ATO

Qu 1. The following statements are possible opinions about Australian's democracy. Please indicate how much you agree or disagree with each statement.

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
In our democracy, we can hold our representatives accountable	[ ]	[ ]	[ ]	[ ]	[ ]

In Australia, the rich have virtually unlimited access to the legal system and the capacity to use it to achieve their own ends	[ ]	[ ]	[ ]	[ ]	[ ]
We have enough input into legislation and the decisions that are important	[ ]	[ ]	[ ]	[ ]	[ ]
Our form of democracy is not perfect, but it beats by a long way any other alternative that we have been shown	[ ]	[ ]	[ ]	[ ]	[ ]

Qu 2. The following statements are possible opinions about the Australian Taxation Office (ATO). Please indicate how much you agree or disagree with each statement

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
The ATO is accountable for what they do	[ ]	[ ]	[ ]	[ ]	[ ]
The ATO respects your privacy	[ ]	[ ]	[ ]	[ ]	[ ]
The ATO explains to you the decisions they make about your tax affairs	[ ]	[ ]	[ ]	[ ]	[ ]
You have the right to an independent review from outside the ATO	[ ]	[ ]	[ ]	[ ]	[ ]

## SECTION B TAX MORALE

Qu 3. The following statements are possible opinions about the tax system and the ATO. Please indicate to what extent you disagree or agree with each statement.

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
Paying taxes gives an	[ ]	[ ]	[ ]	[ ]	[ ]

incentive to engage with the government and political process					
The usage of tax revenues is justified to taxpayers	[ ]	[ ]	[ ]	[ ]	[ ]
Taxpayer's perceive the tax system as fair	[ ]	[ ]	[ ]	[ ]	[ ]
The Tax Office is efficient and public revenues and efficiently translated into public goods	[ ]	[ ]	[ ]	[ ]	[ ]
The tax system is linked to the national strategy of promoting economic growth and wealth	[ ]	[ ]	[ ]	[ ]	[ ]

**SECTION C AUSTRALIA'S ECONOMIC GROWTH**

Qu 4. The following statements are possible opinions about Australia's economy. Please indicate to what extent you disagree or agree with each statement.

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
Australia is a growing economy	[ ]	[ ]	[ ]	[ ]	[ ]
We are experiencing rapid population growth	[ ]	[ ]	[ ]	[ ]	[ ]
We have access to good health care	[ ]	[ ]	[ ]	[ ]	[ ]
Those under financial pressure have access to welfare	[ ]	[ ]	[ ]	[ ]	[ ]
Our property rights are protected	[ ]	[ ]	[ ]	[ ]	[ ]
Higher revenue results in	[ ]	[ ]	[ ]	[ ]	[ ]

better public goods, increased development and state building					
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**SECTION D TAX PAYER MORALS**

Qu 5. The following are questions asking your opinion. Please indicate what your opinion is in relation to each question.

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
One should honestly declare all income on one's tax return?	[ ]	[ ]	[ ]	[ ]	[ ]
It is acceptable to overstate deductions on one's tax return?	[ ]	[ ]	[ ]	[ ]	[ ]
Working for cash-in-hand payments without paying tax is a trivial offence?	[ ]	[ ]	[ ]	[ ]	[ ]

Qu 6. Imagine yourself in this situation. Your tax agent informs you that he or she is unsure about whether one of your expenses is deductible on your tax return, as the tax law relating to this expense is ambiguous. Please indicate how you would react in this situation.

	Very Unlikely	Unlikely	Neutral	Likely	Very Likely
Would you instruct your tax agent to claim the deduction?	[ ]	[ ]	[ ]	[ ]	[ ]
Based on your tax agent's advice NOT TO claim the ambiguous deduction, would you continue to use this agent?	[ ]	[ ]	[ ]	[ ]	[ ]
Based on your tax agent's advice to claim the	[ ]	[ ]	[ ]	[ ]	[ ]

ambiguous deduction, would you continue to use this agent?					
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Qu 7. Now please assume you are the business owner and you had to pay a substantial fine or penalty. How likely is it that you would?

	Very Unlikely	Unlikely	Neutral	Likely	Very Likely
Feel that what you had done was wrong	[ ]	[ ]	[ ]	[ ]	[ ]
Feel sorry/ Remorseful	[ ]	[ ]	[ ]	[ ]	[ ]
Resent the ATO having control over you	[ ]	[ ]	[ ]	[ ]	[ ]

## SECTION E ATO EFFICIENCY

Qu 8. The following statements are possible opinions about the tax system and the ATO. Please indicate to what extent you disagree or agree with each statement.

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
The risk of tax audit is high	[ ]	[ ]	[ ]	[ ]	[ ]
If a business taxpayer is audited, the risk of being detected for tax avoidance or tax evasion is high	[ ]	[ ]	[ ]	[ ]	[ ]
The ATO cannot do much if a large company decides to defy it	[ ]	[ ]	[ ]	[ ]	[ ]
The ATO cannot do much if a small business decides to defy it	[ ]	[ ]	[ ]	[ ]	[ ]

Qu 9. Imagine yourself in this situation. You negotiate discounts for customers in return for being paid in cash. As a result, you are able to reduce tax illegally by \$10,000.

	Very Unlikely	Unlikely	Neutral	Likely	Very Likely
What do you think the chances are that you will get caught?	[ ]	[ ]	[ ]	[ ]	[ ]

**SECTION F CASH BUSINESSES**

Qu 10. As a percentage of total revenue in your business, how much revenue is collected in cash?

0% - 20%	20% - 40%	40% - 60%	60% - 80%	80% - 100%
[ ]	[ ]	[ ]	[ ]	[ ]

Qu 11. How much did your business earn in cash in hand payments over the last 12 months? By cash in hand we mean cash money that you did not pay tax on.

Zero	Over \$1000	Over \$5,000	Over \$50,000	Over \$100,000
[ ]	[ ]	[ ]	[ ]	[ ]

Qu 12. As a percentage, how much of your business income did you declare to the ATO during the last financial year?

0% - 20%	20% - 40%	40% - 60%	60% - 80%	80% - 100%
[ ]	[ ]	[ ]	[ ]	[ ]

Qu 13. How much opportunity have you had to illegally reduce your business tax through cash transactions?

No opportunities	Very Little Opportunity	Little Opportunity	Some Opportunity	Considerable Opportunity
[ ]	[ ]	[ ]	[ ]	[ ]

Qu 14. In your opinion, do the following groups have many opportunities to reduce their tax illegally through cash transactions?

	Strongly Disagree	Disagree	Neutral	Agree	Stongly Agree
Small businesses	[ ]	[ ]	[ ]	[ ]	[ ]

(businesses employing up to 20 people)					
Medium businesses (businesses employing between 20 and 199 people)	[ ]	[ ]	[ ]	[ ]	[ ]
Large businesses (businesses employing 200 or more people).	[ ]	[ ]	[ ]	[ ]	[ ]

### SECTION G KNOWLEDGE OF THE TAX LAW

Q 15. How much information about tax issues do you receive from the following sources?

	None	Not Very Much	Some	A Considerable Amount	Too Much
The ATO	[ ]	[ ]	[ ]	[ ]	[ ]
Tax Practitioners	[ ]	[ ]	[ ]	[ ]	[ ]
Work Related Publications	[ ]	[ ]	[ ]	[ ]	[ ]
TV, Radio, Newspapers	[ ]	[ ]	[ ]	[ ]	[ ]
Friends/ Family	[ ]	[ ]	[ ]	[ ]	[ ]

Q 16. Think about the source which you considered most informative. How much information did you receive on the following?

	None	Little	Some	Considerable Amount	Too Much
How to do your tax return	[ ]	[ ]	[ ]	[ ]	[ ]
What will trigger an audit	[ ]	[ ]	[ ]	[ ]	[ ]
What the penalties are for evasion	[ ]	[ ]	[ ]	[ ]	[ ]
People outwitting the ATO	[ ]	[ ]	[ ]	[ ]	[ ]

Qu 17. Do you think that you have enough knowledge of tax law to meet your businesses obligations to the ATO?

Never	Sometimes	Neutral	Usually	Always
[ ]	[ ]	[ ]	[ ]	[ ]

Qu 18. Did you rely on a tax agent or advisor (tax accountant or lawyer) in preparing your businesses most recent income tax return?

No	[ ] (Skip to Qu 20)
Yes	[ ] (Continue to Qu. 19)

Qu 19. What is your primary reason for using a tax agent?

	Very Unlikely	Unlikely	Neutral	Likely	Very Likely
Fear of making a mistake	[ ]	[ ]	[ ]	[ ]	[ ]
The tax system is too complex	[ ]	[ ]	[ ]	[ ]	[ ]
Insufficient time to prepare my own return	[ ]	[ ]	[ ]	[ ]	[ ]
To legitimately minimise the tax I had to pay	[ ]	[ ]	[ ]	[ ]	[ ]
To avoid paying tax	[ ]	[ ]	[ ]	[ ]	[ ]

## SECTION H SOME OTHER ISSUES

Qu 20. To what extent do you agree or disagree with the following statements given your businesses current situation.

	Strongly Disagree	Disagree	Neutral	Agree	Strongly Agree
Paying tax removes the incentive to earn more income	[ ]	[ ]	[ ]	[ ]	[ ]
Paying tax means that the business just cannot get ahead	[ ]	[ ]	[ ]	[ ]	[ ]

The prospect of tough penalties would deter people from evading tax	[ ]	[ ]	[ ]	[ ]	[ ]
The costs of complying with tax law are too high	[ ]	[ ]	[ ]	[ ]	[ ]
If my peers evade tax then I am more likely to	[ ]	[ ]	[ ]	[ ]	[ ]

## SECTION I TAXPAYER DEMOGRAPHICS

Qu 21. What category of business taxpayer are you? PLEASE TICK ONE BOX ONLY.

Small business (businesses employing up to 20 people)	[ ]
Medium business (businesses employing between 20 and 199 people)	[ ]
Large business (businesses employing 200 or more people).	[ ]

Qu. 22. This section asks questions about you. These characteristics are very important to our research on how different people in different circumstances feel about tax issues.

What is your gender?

What is your age in years?

What was the highest level of education you completed?

What is your current occupation?

How much personal income do you make per annum?

Thank you for taking the time to fill out this questionnaire. Your cooperation is much appreciated.