ORGANISATIONAL CAPACITY FOR RESPONSIVE REGULATION

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Abstract

In April 1998, the Australian Taxation Office (Tax Office) adopted a policy of responsive regulation of tax compliance by small firms in the building and construction industry. Known as the Australian Taxation Office Compliance Model (ATO Compliance Model), the new approach is grounded in past research into regulation of business entities. As seen by its promoters, it promises to improve significantly tax compliance in the cash economy. Drawing from survey and interview data, we explore the Tax Office’s capacity for successful implementation of the ATO Compliance Model. Specifically, we examine the extent to which it had the leadership and staff commitment to implement the policy successfully. We also explore whether or not project field-level staff saw merit in the program and eventually came to support it. We conclude by examining whether the owners of small building and construction firms changed their perspectives on the Tax Office and tax compliance following introduction of the ATO Compliance Model.
Organisational capacity for responsive regulation

Neal Shover, Jenny Job and Anne Carroll

In July 1997 the Australian Taxation Office (Tax Office) launched a series of initiatives aimed at the cash economy. The cash economy is understood as income that is not recorded in the books from which the tax return is prepared (Cash Economy Task Force, 1998, p. 15). The Tax Office initiatives targeted cash economy transactions by small firms in several industries. Several months later, they were augmented by a Tax Office decision to adopt a new approach to tax enforcement and to try it out in the small building and construction industry. This program of responsive regulation, known as the Australian Taxation Office Compliance Model (ATO Compliance Model), reflects considerable research into regulatory processes and is touted as a more effective approach to tax enforcement. It has since been extended to all of the Tax Office’s operations.

At inception, this research was intended as a retrospective process analysis of implementation of the ATO Compliance Model for the small building and construction industry, and an examination of some of its short-term impacts. Process analysis is used in evaluation research as a way of understanding how reforms are implemented and brought to bear in the day-to-day work routines of managers and employees (Weiss, 1998). It can lay bare how organisational realities and dynamics constrain reforms adopted in other circumstances for reasons often unknown to or unappreciated by those charged with implementing them. Typically, process analysis uses interviews and observation as a way of interpreting the statistically observable consequences of a new program.

Twenty months after its inauguration, the impending arrival of the goods and services tax (GST) caused a substantial reduction in personnel and resources committed to the Cash Economy Building and Construction Project (CE/B&C project). This also caused us to scale back our original research plans and shift our focus somewhat to examining the Tax Office’s capacity to effectively implement the ATO Compliance Model.
This paper begins with a brief description of the genesis of the ATO Compliance Model and its adoption by the Tax Office. This is followed by a description of the underlying assumptions and objectives of the present study, and the methods it used. Our focus is organisational capacity. This is defined as the extent to which an organisation possesses the mandate, requisite resources, determination and facilitative environmental conditions to implement reform policies, with fidelity to the goals envisioned by reformers. The research findings are then presented, drawing heavily from analysis of the perspectives and experiences of field-level personnel.

The paper concludes with analysis and discussion of data gathered from interviews with owners of small building and construction firms.

**Background**

The closing decades of the twentieth century saw significant policy developments in the movement to enhance business compliance with regulatory rules (Parker, 2000). Previously, the ‘command-and-control’ approach dominated discussions of and proposals for enhanced regulation. This approach incorporates legal threats, inspections and the mechanical imposition of penalties for non-compliance. A variety of evidence suggests, however, that the adversarial nature of command-and-control regulation fosters resentment, mistrust and resistance, at least in some industries or industry sectors. Persistent doubts about its benefits and effectiveness eventually led to programs of enforced self-regulation and cooperative regulation. These are distinguished both by shared state–corporate responsibility for enforcement and by a wider range of official options for responding to non-compliance. Proposals for and programs of enforced self-regulation also came under fire by critics who question whether they can deliver fairer or more effective outcomes.

This controversy led Ayres and Braithwaite (1992) to propose a convergence of the two approaches, known as ‘responsive regulation’. Responsive regulation is grounded in a hierarchical development and application of enforcement strategies that take into account the circumstances and capabilities of differing business entities. It is ‘distinguished….both in what triggers a regulatory response and what the regulatory response will be’ (Ayres & Braithwaite, 1992, p. 4).
Conceptually, Ayres and Braithwaite (1992) present their notion of responsive regulation in the form of a ‘regulatory pyramid’, which is depicted graphically in Figure 1.

Figure 1: Regulatory pyramid.

The base of the pyramid is made up of broad cooperative strategies of self-regulation that emphasise education about rules and provide assistance with complying. For citizens and businesses that fail to comply despite educative and cooperative actions, officials may escalate their responses and sanctions. The top of the sanctions pyramid is represented by a ‘benign big gun’. Ordinarily kept in the background, it represents the most severe sanctions in the arsenal of regulatory officials. The availability of the benign big gun, coupled with officials’ clear willingness to employ it, serves to push enforcement down towards the base for those who fail to respond to assistance, or to punish those who commit an offence beyond deterrence or refuse to cooperate. This approach to regulation nurtures voluntary compliance while displaying a willingness to employ escalating sanctions should the need arise.

Ayres and Braithwaite (1992, p. 4) suggest that officials ‘be responsive to industry structure in that different structures will be conducive to different degrees and forms of regulation’. More specifically, effective responsive regulation requires that officials understand and take account of the diverse motivational sources (‘drivers’) of non-compliance. These are not well understood at present, but the ATO Compliance Model incorporates the results of previous
research that points to four common motivational postures (Braithwaite, 1995). The results also define the nature of the regulator–client relationship: managerial accommodation (incorporation of the firm’s own strategies to achieve compliance); capture (acceptance and identity with the regulatory system); resistance (confrontation and challenge of regulations); and disengagement (withdrawal from the regulatory process).

Advocates for responsive regulation contend that motivations for non-compliance are not fixed and immutable, but are subject to shift within the dynamics of the regulatory process. Movement in the direction of compliance may be accomplished by engaging the owners or managers of firms in a common regulatory culture with strong social bonds and a shared mission. This assumes that failure to comply may not result only from wilfulness but also from ignorance of what is required, from inadvertent errors in tax records, or from changes in taxpayers’ circumstances. In such cases they are not necessarily resistant or disengaged from the tax system. Understanding both the diverse motivational sources of non-compliance and the need for mutual respect and trust in contacts with firms is central to improving compliance. Thus, firms whose owners or managers are inclined to comply with the law may be strengthened in this posture by officials who treat them as trustworthy, if confused or misguided citizens, while those of a more resistive bent may be nudged towards compliance through the judicious use of educative efforts laced with a dose of threat. The more recalcitrant are another matter, for they may need to be reminded of, or even to experience first-hand, criminal prosecution or loss of their licence to do business.

Notions of responsive regulation grew out of a substantial body of empirical research into the regulatory process. Whilst they have considerable intuitive appeal, particularly when applied to the dynamics of interpersonal relations, as yet they have been subjected to limited testing. The consequences of responsive regulation, when entrusted to the potential distorting influences caused by bureaucratic considerations and dynamics, remain unclear. Responsive regulation, moreover, may work well in some circumstances but not nearly so well in others; policies that are effective with small firms may have quite different effects when employed with large, heavily resourced entities and industries. Thus the need, as recognised by its proponents, to examine the effects of responsive regulation in diverse circumstances and locales. Research into industry-specific cultures and practices is an important step in identifying effective regulatory strategies.
The proportionate distribution of motivational postures is rooted in conditions and understandings that vary both spatially and temporally. Put differently, industries, regions and time periods may have considerably different mixes of motivational postures. A host of economic, sociological, cultural and psychological factors condition the ways typical firms see and interact with regulatory agencies and personnel. Where the Tax Office is concerned, this constellation of factors, known as BISEPS (Business; Industry; Sociological; Economic; Psychological factors), shape the capacity and inclination of firms to comply with tax requirements. Table 1 lists the significant BISEPS factors for small building and construction firms.

Table 1: Tax Office – Building and construction BISEPS

The following are taken from 1996 Tax Office statistical data, Australian Bureau of Statistics figures and the Building and Construction Leaders Workshop held in April 1998. Some of the following factors may overlap in category but have been placed in one BISEP factor.

Business factors

- Key players are professions/suppliers/associations
- Core group of contractors/subbies/illegal subbies
- Flexible status – easy to become contractor
- Low membership in industry associations
- Variable record keeping standards
- Minimal regulations in some trades
- Word of mouth – advertising
- Minimal written contracts
- Part-time tradesmen
- Low set-up costs
- Competitive
- Status of worker
- Number of businesses = 239,475
  - Individuals – 46.8%
  - Partnerships – 30.7%
  - Companies – 16.3%
  - Trusts – 6.2%
- 36% have employment variation reviews (EVRs)
- 59,000 are group employers
- 98% returns prepared by tax agents
- 280,000 are salary and wage earners, with an average salary of $26,000
- Contributed $41.4b total business income
- Paid $816m in tax (2%)
- Tax debt approximately $62m
- Information technology – $21m, Contracted services – $17m, PPS – $16m
**Industry factors**

- Cash prevalent in some areas/consumer attitude
- Recognised hourly rates/metre rate
- Variable skill levels and supply
- Varying licensing requirements
- Flexible working patterns
- Low profit margins
- Government and other regulations
- Industry-based training
- Location differences
- Status of workers
- Highly unionised-commercial
- Market segments
- Pay As You Earn (PAYE) erosion
- Used to Prescribed Payments System (PPS)
- Credit-based
- Barter

**Sociological factors**

- 50% = 35 to 54 years
- 86% of industry are male
- Low levels of literacy
- 10% = Child Support Agency clients (population average = 5%)
- Norms – weekends are for cash
- Male does labour, wife keeps books
- Ethic of looking after each other/Jobs for mates
- Not paying tax is ok – generally
- Ethic of not ripping each other off
- Government is the enemy/red tape/big brother
- Cultural: distrust of government
- Ignorance of requirements
- Manual work/pub mentality

**Economic factors**

- International investment
- International crises (for example Asia)
- Growth leads to complexities/costs
- Currently in growth after long depression
- Population growth/migration
- Inflation and interest rates
- Peaks and troughs
- Economic uncertainty
- Weather
- Home ownership/Australian culture/affordability
- PPS system not effective
- Regional/patchy activity
- All governments – policies, laws, reforms, costs, etc.
- Unemployment and sickness benefits (USB) and cash
- Industrial disputes
Psychological factors

- Fear of the Tax Office
- Greed
- Attitude – the challenge/game/gamble
- Folk hero/Ned Kelly if you cheat
- Peer pressure apprentices up
- How government spends
- They are victims
- Paperwork overload
- Cash jobs
- ‘I’m in charge’
- Level playing field/fairness

The use of BISEPS materials enables Tax Office and other regulatory agencies to make use of industry-specific information that might require a particular strategy. It also strengthens awareness of both current and future challenges and enables forward planning to meet the needs of both the industry and the Tax Office. The Building and Construction BISEPS in Table 1 outline aspects of the Australian small building and construction industry circa 1998. There is little reason to believe matters have changed significantly since then.

Life in the small building and construction industry is filled with uncertainties, although the participants are a fairly casual lot who are prepared to take risks but are also content to remain as small businesses. This is an industry dominated by males with low literacy levels and variable skill levels, many of whom come from non-English speaking backgrounds. Distrust of government and fear of the Tax Office are common. Generally it is considered OK to not pay tax, and peer pressure contributes to many taking the risk of cheating on their taxes. Business relationships are characterised by informality; written contracts are eschewed, and a great deal of advertising is by word of mouth. Trade regulation is minimal and licensing requirements vary. These are independent people who like to manage their own show. Nearly half of these business owners are sole traders, and nearly a third are in partnership, commonly with their wife. The overwhelming majority of them use the services of tax agents, but few maintain ongoing relationships with their tax agent throughout the year. The business records are maintained by the wives. This industry is often faced with economic uncertainty and pressures from international competition, inflation and interest rates, and the weather. Barter is common, as is the use of cash. The industry norm is that
weekend work is paid for in cash that is not declared as income. The industry ethic is very much one of looking after each other, and the high level of union membership illustrates this. There is a strong belief in the ‘level playing field’, meaning that everyone in the industry should have an equal chance to make a living. This description illustrates the competitive but close relationships in this industry. It also highlights the need for different ways of communicating with the small building and construction industry rather than the ‘usual’ habit of government agencies to communicate by form letters couched in the language of petty officialdom.

The ATO Compliance Model

Adoption of a strategy of responsive regulation by Tax Office executives was the culmination of nearly two years work by a Cash Economy Task Force. Formed in 1996 and comprising representatives from industry, community groups and government, the Task Force worked in partnership with the Tax Office to develop an understanding of the cash economy and potential responses to it. The Task Force issued its initial report in 1997, which was followed by a series of Tax Office initiatives aimed at cash transactions among small businesses in building and construction, restaurants and cafes, fruit and vegetables, clothing and taxis. Regional projects were aimed at other industries, including fishing, computing and road transport. By 1998 more than 900 Tax Office employees were assigned to cash economy projects.

In April 1998 the Commissioner of Taxation publicly released a second Cash Economy Task Force report. It featured the ATO Compliance Model and its principles, together with suggestions on ways the Tax Office could tackle the cash economy. The Commissioner also announced that the CE/B&C project would begin using the principles of the ATO Compliance Model. Adoption of the ATO Compliance Model set a new direction for the Tax Office, as well as expectations of how it would shape and manage the tax system. Eventually, more than 3000 Tax Office staff were trained in the ATO Compliance Model, and it was implemented in a range of initiatives. Before the number of personnel assigned to the CE/B&C project was reduced in 1999, some 200 Tax Office personnel were assigned to it.
Organised in teams of 10 to 15, they were located in major metropolitan areas throughout Australia. A graphic depiction of the ATO Compliance Model is presented in Figure 2.1

Figure 2: The ATO Compliance Model.

Every approach to regulation features a somewhat distinctive technology. Audits are a key component of command-and-control tax regulation. The audit process highlights the importance of monitoring individuals and business entities in order to uncover violations of law. Accusation and confrontation are unavoidable by-products of this technology. Audits can require months to complete. Those found to be non-compliant are assessed penalties which presumably serve to remind them and others that compliance is the best way to go. Not surprisingly, agencies operating in this fashion are frequently seen as high-handed adversaries by citizens subject to their programs (Braithwaite, Walker & Grabosky, 1987). Historically, the Tax Office operated this way, generating large numbers of prosecutions, the bulk of which were directed at taxpayers of modest means (Grabosky & Braithwaite, 1986).

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1 Several months before it adopted the ATO Compliance Model, the Tax Office issued a *Taxpayers' Charter* (Australian Taxation Office, 1997). Seen as a covenant with taxpayers, it spells out their rights and obligations, and the options available to them should they be dissatisfied with their treatment by the Tax Office.
Adoption of the ATO Compliance Model caused the Tax Office to develop and train its staff in a technology of compliance that contrasts in several ways from the one they used previously. Whilst maintaining audits as part of the compliance assurance arsenal, the ATO Compliance Model, as developed by the Tax Office, features a technology designated ‘real time reviews’. The objectives here are more ambitious than a search for violations and assessment of penalties. Whereas audits typically require detailed examination of a firm’s records over a period of months or even years, real time reviews are generally limited to examining business records and activities for the preceding three months. They require less time than traditional audits. Real time reviews have a strong educative focus: they are employed not only to uncover evidence of non-compliance but also to increase understanding of proper bookkeeping practices and how to increase future compliance. Taxpayers are treated according to their individual circumstances and, where significant discrepancies are identified, they are advised and invited to review and amend their previous tax returns. The focus is on the probability of future compliance. Real time reviews also allow Tax Office field officers to refer cases for audit or prosecution when wilful or egregious non-compliance is detected. The use of real time reviews allows field staff to achieve greater coverage and visibility in the business community. It also enables Tax Office personnel to garner intelligence about specific industries (Australian Taxation Office, 1999b; 1999c). One measure of the Tax Office’s commitment to the new technology is that 7515 real time reviews were conducted for a two-year period from 1998 to 1999 (Cash Economy Project, 1999, p. 3).

**Objectives**

Reformers cannot assume their intentions and plans will meet with committed and faithful implementation. Bureaucracies charged with implementing reform policies can show a highly varied capacity for the job at hand:

Policy ideas that sound great in theory often fail under conditions of actual field implementation. The implementation process has a life of its own. It is acted out through large and inflexible administrative systems and is distorted by bureaucratic interests. Policies that emerge in practice can diverge, even substantially, from policies as designed and adopted (Bardach, 2000, p. 25).
Doubtless it was recognition of this that led the Cash Economy Task Force to emphasise as constraints on the implementation and impact of reform ‘attributes of the tax regime and administration’. These include not only tax legislation but also ‘its administration, and Tax Office cultural factors’ (Cash Economy Task Force, 1997, p. 6).

Clearly, organisations vary in their capacity for effective implementation of specific reform policies and programs. Assuming sufficient understanding, commitment and organisational resources, there is reason for optimism. If one or more of these conditions is absent, it is doubtful a new policy can be instituted without serious departures from the vision of the reformers. This includes routine procedures for monitoring the short-term consequences of reforms as another component of organisational capacity.

All organisations are constrained by a variety of characteristics and conditions that affect their capacity to adopt and implement reform initiatives. Some are environmental, others are matters of staff and organisation, and still others are grounded in the kind of reception reforms receive from affected constituencies. This research examines the reception given the ATO Compliance Model by its front-line personnel. Is there evidence to suggest that, whatever their initial response to the ATO Compliance Model, they moved in the direction of increased understanding and support for its principles and procedures? A secondary objective of the research is to explore business awareness of and opinions about the Tax Office’s changed operating procedures.

Assumptions

Following the Tax Office decision to scale back the CE/B&C project and our decision to terminate research earlier than originally planned, data analysis was guided by four assumptions about the kinds of short-term changes one should reasonably expect if the Tax Office possessed or acquired appropriate and sufficient capacity to implement the ATO Compliance Model successfully. First, there should be evidence that senior leadership of the Tax Office supports and invests in the reform policy. Without this condition, there is little reason to believe that mid-level managers, their field-level counterparts and front-line staff will take its prescriptions seriously, and change their behaviour accordingly. There should be evidence, moreover, that leadership has planned for and put in place from the outset
mechanisms for monitoring early implementation and subsequent evaluation of the initiative. Doing so ensures the intelligence needed to assess progress or the lack of it, and to make short-term corrections to the implementation process.

Second, the policy, as defined and presented to supervisors and front-line personnel, should neither conflict nor be cognitively incongruent with their current perspectives and practices. Third, there should be evidence that as they are trained and acquire experience with the new policy, they move in the direction of increased understanding and support for it.

Finally, the context and times should be conducive to or permissive of reform. Whilst probably few reforms are undertaken in placid times, typically there seems little reason for change in these circumstances - a calm environment lends itself to the deliberate and self-reflective decision-making that can nurture and sustain through the precarious early days. By contrast, reforms undertaken in times of turbulence and tension may not permit personnel to focus on the job at hand or to reflect upon and make use of evaluations. Times of turmoil do not permit calm, deliberative decision-making.

Because the ATO Compliance Model posits complex and slow-developing long-term relationships between the behaviour of enforcement officials and the responses of taxpayers, it was recognised at the outset that an adequate evaluation of the CE/B&C project would require collection of data over several years. Unfortunately, the short follow-up period available to those charged with examining the impact of the ATO Compliance Model permits confident conclusions about few if any consequences of its adoption and use for nearly two years. Our examination of the impact of the CE/B&C project, by contrast, is short-term and based on samples of limited or dubious generalisability. The limitations of the samples and methodologies further reduce the level of confidence in the findings.

Method

Our research commenced some 18 months after the ATO Compliance Model was adopted by the Tax Office leadership and was added to ongoing initiatives aimed at the cash economy. We planned to collect a variety of data on the Tax Office’s implementation of the ATO Compliance Model, as well as evidence of some of its short-term impacts. We assumed that
by using a variety of methods and collecting a variety of data, findings gained from multiple methods or sources would compensate to some extent for their individual shortcomings. We were only partially successful, however, principally because data collection was terminated prematurely when cash economy personnel were shifted to work on the GST. This necessitated a change in plans, and our analytic focus now shifted to examining the capacity of the Tax Office to successfully implement the ATO Compliance Model.

Data were collected over a 10-month period (August 1999 through May 2000). We began with interviews during August 1999 with 15 Tax Office managers or employees – some face-to-face interviews and others by long-distance telephone. These conversations, averaging approximately 25 minutes, helped familiarise the senior author with the Tax Office and provided an opportunity to talk with several managers who played important roles in the field-level implementation process. This was followed in November–December 1999 by visits to five Tax Office offices where significant CE/B&C project initiatives were in operation (Sydney CBD, Parramatta, Penrith, Box Hill and Dandenong). We interviewed 26 field-level managers and operatives about their experiences with and opinions about the ATO Compliance Model in the building and construction industry. The semi-structured interviews followed a topical guide and averaged approximately 35 minutes each. All were tape-recorded and transcribed for subsequent analysis.

Following these interviews, in May–August 2000 a survey instrument was emailed to all Tax Office personnel who at any time were assigned to the CE/B&C project. After two follow-up reminders to the 260 persons who were sent surveys, 32% returned surveys to us. This low response rate leaves us unable to assume confidently that those who returned surveys represent all involved in the CE/B&C project.²

² Although we can only speculate as to the reasons for the low response rate, the timing of the survey was unfortunate: by the time it was mailed to Tax Office staff, the CE/B&C project had been scaled back substantially. The ATO Compliance Model was no longer a salient issue or focus of work routines, and many Tax Office staff may have stopped caring about their experiences using it. In addition, the volume of email field-level staff receive daily is both sizeable and increasing, and this may make it easy to overlook or ignore messages that clearly do not require a response. The average age of the 84 survey respondents was 42.6 years, and the average length of time they were assigned to the CE/B&C project was 22.6 months. Women comprise 21% of the respondents. When asked if they had worked as a supervisor at any time during the project, 34.6% of respondents answered affirmatively.
During May–June 2000 we interviewed the owners of 27 small building and construction firms in Melbourne and Adelaide. The semi-structured interviews, which were tape-recorded for subsequent transcription and analysis, averaged approximately 30 minutes and explored respondents’ experiences with and beliefs about the Tax Office and its operations. They were focused primarily on respondents’ contacts with the Tax Office in the years immediately before and after introduction of the ATO Compliance Model in 1997.

A variety of difficulties left us unable to follow through with original plans to interview equal numbers of firms/owners who had varying degrees of contact with the Tax Office in the preceding two years. Among them, we were unsuccessful in obtaining telephone numbers for many firms listed in Tax Office files, and a substantial majority of those we did contact declined our request for an interview. We estimate that not more than 5% of all firms contacted agreed to and completed an interview. As a result, the sample of businesses almost certainly is tilted toward those who comply with tax requirements and have no particular reason, therefore, to be wary of sharing their experiences with and opinions of the Tax Office. Thus we almost certainly interviewed a sample of firms whose owners had good records of voluntary compliance with tax laws. As one of our subjects told us: ‘I think if a company is fair dinkum and up-front, they shouldn’t be worried about the Tax Office, you know. If you’re doing the right thing you’ve got nothing to worry about.’ In the language and logic of the ATO Compliance Model, as presented in Figure 2, these firms and their owners are located near the bottom of the pyramid. Our findings are therefore limited to the population they represent.

In addition to interviews with Tax Office personnel and the owners of small building and construction firms, we also interviewed an executive of the Department of Public Prosecutions and a representative of the Master Builders Association of Victoria. These interviews were also tape-recorded.
Findings

To what extent were our assumptions about organisational capacity for change matched by conditions in the CE/B&C project during the first few years of its operation? Did it have or acquire the resources to suggest that over a longer period the expected results of responsive regulation would be realised?

Leadership and staff

Few presumably would dispute the assumption that a creative and committed staff in sufficient numbers is critical to an organisation’s capacity to faithfully implement reform policies. Ample evidence suggests that senior Tax Office managers gave strong and ongoing support. This support came from the highest levels of the Tax Office, particularly from the Commissioner, the Deputy Commissioner of the Small Business area, the Assistant Commissioner responsible for managing the cash economy initiative, and the Project Leader for Building and Construction. They sponsored and provided resources for training in the ATO Compliance Model for all staff on the CE/B&C project, and they visited and provided encouragement. When the initial training program was begun, senior Tax Office managers signalled their support by attending and participating in the training course. They discussed the direction in which the Tax Office was moving and how the ATO Compliance Model complemented it. They emphasised that Tax Office practices and procedures were important issues in building and maintaining community confidence in the Tax Office and its ability to administer the tax system. None of the personnel we interviewed faulted Tax Office executives for failure to support or to provide sufficient resources for the CE/B&C project. Approximately 35% of our survey respondents indicated that at some time they were responsible for supervising other Tax Office personnel as part of the CE/B&C project. They ranged from team leaders to mid-level managers. All survey respondents were asked to indicate their agreement or disagreement with the statement: ‘The leadership of the Australian Taxation Office failed to devote sufficient resources to implementation of the compliance model’. For supervisors, 33.3% of respondents agreed or agreed strongly whilst 40.7% disagreed or disagreed strongly. For respondents who were not supervisors, the results are 34.6% and 36.5% respectively. These findings are consistent with the interview data: neither supervisors nor operatives perceive a failure by Tax Office executives to provide adequate fiscal resources and personnel for the CE/B&C project.
In this and in other ways, support for the ATO Compliance Model by Tax Office executives was not lost on field-level staff. When asked for his opinion about the ATO Compliance Model, one Tax Office operative spoke with apparent conviction about the importance of treating taxpayers with ‘understanding’, ‘respect’ and ‘compassion’. As the interview progressed, however, and he was asked to reconcile seemingly contradictory statements, he said that his earlier comments reflected a belief that Tax Office executives are committed to the ATO Compliance Model, that they expect field-level staff to get on board, and that they would be watchful for signs of weak commitment and follow through.

This is not to say the ATO Compliance Model was welcomed by all or even by most staff. Some saw it as a hopelessly abstract approach developed by academics and then adopted by Tax Office executives:

Let’s face it: the compliance model was an academic model adapted to the tax situation. It was developed by … I think, people outside of [ATO]. ATO saw it as the way we should be moving … and I’m not disagreeing. I think they’re right. But it was done at the more senior level by people who are inclined that way [toward consultative approaches] anyway.

For most field-level personnel of the Tax Office, adoption of the ATO Compliance Model for the small building and construction industry apparently came out of the blue. For those we interviewed, there was limited awareness of how the decision was made, combined with some disappointment and cynicism:

I’m an employee of the Taxation Office, and this is an instruction that’s put to me. I’ve no input into its adoption whatsoever. I’m not asked whether, you know, this is a good idea. Should we go this way, or whatever? You’re an experienced taxation officer. You’ve been in this place for [more than 25] years, what have you found in that period of time about, you know, compliance in taxation?

This was imposed ... certainly. No two ways about it. We were given two days to provide feedback ... It was like, okay, ‘we’ve made a decision, but we should get something from the people in the office to make them think that they’re having some feedback into it’. [W]e didn’t feel we were part of it at all

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3 Some may see irony in the fact that the ATO Compliance Model, which highlights the importance of and the pay-off from consultation, education and cooperative relationships, was adopted and implemented in a top-down, command-and-control fashion within the Tax Office.
... [T]he decision was made before we even were given a chance to offer feedback. I think they ended up – so many people complained – they gave us another week to give feedback, but it was still basically we felt that they just threw it away or put it in a corner and basically came out with the model they wanted.

For these reasons, perhaps, a mid-level manager who helped implement the ATO Compliance Model told us that:

It wasn’t universally welcomed in the Tax Office, or in the [CE/B&C] project anyway, which is probably representative of the Tax Office. I think the majority of people in the Tax Office thought straight off ‘oh, yeah, now we’re going soft on everyone’, you know. I think that was the quick interpretation of it, that ‘oh, now we just pat them on the head and tell them to be good in the future and walk away’, you know.

The respondent noted further that apparently little thought was given to ‘the ability of people’ (staff) to shift to the new approach. The respondent added: ‘I think it’s a huge jump for some’.

Whatever their initial reactions, however, successful implementation of a reform is enhanced if staff take on as their own its fundamental assumptions. Consequently, in our survey we asked current and former CE/B&C project personnel to comment retrospectively on their expectations about the ATO Compliance Model at introduction and after they gained experience using it. Responses to this series of questions suggest that the subjects fall into three groups. At introduction, 9.8% said they were very sceptical about the ATO Compliance Model whilst 4.7% were equally enthusiastic about it. The remaining 85.6% of respondents ranged from somewhat sceptical to somewhat enthusiastic. Although few of those who held strong opinions about the ATO Compliance Model at introduction changed their assessment with experience, for those with less extreme opinions a majority (54.1%) became more positive about it. Our interview data are consistent with this pattern.

Q: So, you have had two years experience now with the compliance model?
A: Yes.
Q: And what’s your assessment of it now?
A: I like it. I like it. It has a greater impact, because previously you were only dealing, you know, [one-on-one] and had no impact on the industry ... But now, bringing in the various associations and what have you and getting the publicity, it has a wider impact. So it is more one-to-many, which I like. A lot more flexibility, a lot more choice, which I like.
Originally ... it was seen as ‘oh, this is going to be Mickey-Mouse type of activity that they’re going into. When will they get back to doing actual work?’ And things like that. After a while of going through it, they could see the advantages of doing some of the alternative type of work as well as the audit activities. But I think it was only when they could see that there was room for the two.

One reason for change or the lack of it may lie in the perspectives and practices of front-line managers. Of all respondents, supervisors were more likely to have been somewhat or very sceptical at introduction although, like operatives, a majority of them became more supportive of the ATO Compliance Model as they gained experience with it. Nevertheless, when compared with operatives, supervisors were also more likely to become sceptical with the passage of time (18% and 6% respectively).

Their growing support for the ATO Compliance Model does not extend to an unqualified endorsement of it; staff beliefs about and experience with tax enforcement have left many ambivalent about the long-term consequences of responsive regulation. On one hand, they prefer real time reviews to audits. Generally the latter are triggered by suspicion or evidence that something is amiss with the tax behaviour of a business. The resulting detailed examination of financial records can be both adversarial and confrontational. They can be difficult both for operatives and for the targets of their efforts. Several Tax Office operatives we interviewed commented spontaneously on their dislike for the audit process, which puts a premium on being able to act assertively. For example:

While I was an auditor I hated it. When I was doing my degree I always wanted to be an auditor, and it’s like, you know, you get there and you think, ‘this is horrible’. So I didn’t like it. I didn’t like the aggression that came along with auditing. It was more than assertive, it was probably aggressive ... And it was like, let’s see what we can get, how we can intimidate this person, that sort of thing ... So I really learned to hate it a lot. When the Building and Construction Project came along, and we saw the methodology was real time reviews, we didn’t know what it meant. But when we saw that it was a lot softer than an audit, a lot faster, and less intimidatory, and probably more helpful, I liked it. I preferred that way of doing things.

On the other hand, former CE/B&C project staff members tend to be rather cynical about the sources of tax compliance. Asked, for example, whether ‘fear of penalties is more important than conscience and the obligations of citizenship’ as reasons for tax compliance, 71.8% of
our survey respondents agreed or agreed strongly. Clearly, they believe that a strong threat is fundamental to the compliance assurance process. Not surprising, therefore, one of their most frequently mentioned concerns was whether the Tax Office would maintain the level of prosecutions needed to make it work. They wonder whether the ‘benign big gun’ will be employed sufficiently often to maintain an acceptable level of tax compliance.

The technology of compliance does not end with real time reviews; responsive regulation highlights the importance of involving community and industry groups in efforts to maintain or improve overall tax compliance. This means that Tax Office staff are now expected to also contact and work with these stakeholders to improve awareness of and support for the tax system. This requires work routines and personal skills different from those used in audits and penalties, the traditional mainstays of tax enforcement. Early on in the CE/B&C project, the project leader visited the senior management of the Master Builders Association and the Housing Industry Association in Canberra. He explained that the project would be using the principles of the ATO Compliance Model, and outlined the benefits its use would bring to the Tax Office and to the building and construction industry. Similar meetings were held with the management of comparable associations around Australia. The new efforts bore fruit. The Master Builders Association announced its support for the work the Tax Office was doing in the industry and its willingness to work with the Tax Office to ensure cash economy practices were ended (Australian Taxation Office, 1999a). It is premature to examine the effects of these complex and indirect effects of responsive regulation, but field-level Tax Office personnel who responded to our survey were notably positive in their assessments of how well this process proceeded and the pay-offs from it. Specifically, they were asked to indicate their degree of agreement or disagreement with the statement: ‘During the time I worked in the Cash Economy Building and Construction project, I witnessed substantially improved trust and cooperation between trade associations and the Australian Taxation Office’. A majority of respondents (51%) agreed or agreed strongly.

Whilst the broad principles of the ATO Compliance Model are endorsed by our subjects, this begs the question whether their increasing support for it in the abstract reflects detailed understanding of its principles and whether they in fact changed their work routines accordingly. Concern about these matters is heightened by comments we repeatedly heard to wit: it is ‘just common sense’ or ‘it’s what we’ve been doing all along’. This suggests that the
more arcane aspects of the ATO Compliance Model may have been missed by a substantial proportion of those assigned to the CE/B&C project. A team leader told us:

[I]t’s really interesting. When we did our one-to-one session, and even afterwards, one of my team members said to me [that] he wished he knew about this compliance model previously. Because it’s not just a tool you can use in your work environment, it’s a tool you can use in real life, you know, in your relationships with other people. I mean you give people a chance before you go heavy with them. It’s what we’ve always done but all you’ve done now is put a name to it. You call it a compliance model. It’s what we always used to do.

The subject now acknowledged that his earlier characterisation of the model masked considerable doubt and uncertainty about it.4

**Context and timing**

We noted that favourable environmental conditions can play a critical part in an organisation’s capacity to change policy directions and to construct viable new structures and practices. Use of the ATO Compliance Model was added to an ongoing series of Tax Office initiatives begun in 1997 that were aimed at increasing citizen trust and reducing cash transactions in several industries. These initiatives came in the midst of what seemed to some of those we interviewed as a period of torrential changes, nearly all of which necessitated change in work routines and skills. To this was added later the inexorable approach of the GST. By mid-1999, when we interviewed Tax Office operatives, expressions of anxiety and fear of being overwhelmed were commonplace. For example:

Our workload has increased. Our responsibilities have increased ... The knowledge that you require to do your job properly is increasing ... The biggest change in the Tax Office I’ve seen [however] is because of technology, not because of the compliance model ... I’m not the best person when it comes to technology. It’s going too fast for me ... and I’m more reluctant to change ... Now we’ve got the new tax system, and it is coming on top of everything else. And I just don’t want to know about it yet. I really don’t. I don’t want to know anything about GST.

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4 In 30 years research, the senior author has rarely encountered the level of unease and anxiety expressed in interviews with Tax Office field-level personnel. Whether this results from unfamiliarity with academic investigators or from the pace of change in their workday, many of those we interviewed seemed unusually jittery.
The subject is not alone in his perceptions and anxiety. Responding to twin imperatives of the push for improved efficiency provided by rapid technological change and new tax policy, the result is a marked increase in workload and efficiency by Tax Office personnel (Commissioner of Taxation, 2000, pp. 13–14). Along with outsourcing of work formerly carried out by government employees, hotelling or ‘hot desking’ has changed forever the nature of operatives’ work and their interaction with supervisors and headquarters; a great deal of this now takes place electronically. For many front-line employees, one of the principal consequences is a sense of mistrust and anxiety, to which the rapid approach of the GST was a major contributor.

**Evaluation**

The Tax Office evaluated its cash economy projects and reported evidence that things are working (Australian Taxation Office, 1999a). Evidence of two kinds is cited in support of this conclusion: gains in income and reported taxes by building and construction firms, and the results of an ongoing series of surveys in which citizens are asked their perceptions of the Tax Office and its operations (Commissioner of Taxation, 2000, pp. 35–6). Both are reasonable and appropriate measures of program impact: the former because use of the ATO Compliance Model clearly is meant to increase taxpaying, and the latter because the new Tax Office in time should be seen by citizens as a more helpful and less threatening arm of government.

No data or evidence used or cited to this point as evidence of success can stand cursory methodological scrutiny, however. Although reported income is up, this increase must be seen against the backdrop of economic improvement and the upward trend in tax revenues. ‘For most of the past decade, total and company tax collections have grown at a rate greater than GDP’ (Commissioner of Taxation, 2000, p. 9). Since December 1996 the Tax Office has conducted biannual surveys to measure community perceptions of the organisation. Whilst citizen perceptions of some aspects of Tax Office operations have improved modestly over the past three years, ‘the results to date have remained fairly constant’ (Commissioner of Taxation, 2000, p. 49). Studies of samples drawn from the building and construction industry have been more promising, but failure to examine the possible influence of other factors limits confidence in these findings. The short period of time (three years) is not sufficient to warrant more than cautious optimism.
**Business owners and the ‘New Tax Office’**

Underlying our interviews with the owners of small building and construction firms is the assumption that if the ATO Compliance Model is on the right track, there should be evidence that the word is getting out to those at whom the policy is aimed and evidence also that they are changing their perspectives. Specifically, we reasoned that if any short-term impacts of the CE/B&C project were to be apparent after less than two years duration, it should be present in the experiences and opinions of business owners who had direct contact with the Tax Office during this time.

Before examining this issue, it is noteworthy that very few of those we interviewed expressed opinions of unfairness about the tax system generally. One respondent, however, told us:

> [T]he thing that you’ll find in the building industry is that they are particularly hostile to the Taxation Department because they sit there and they watch multinational companies paying no bloody tax at all [whilst] they are being screwed into the ground. That’s where the hostility comes from. That’s where a lot of the cash economy comes from, because there ... is resentment ... The rates are too high, [and] multinationals will not pay their taxes. And not only multinationals, there are others too. But generally the wealthy don’t pay their bloody taxes, and that’s where the resentment comes from.

Q: What ... could the Tax Office do to soften this perception of unfairness in the taxation system?
A: Charge multinational companies exactly the same rate of tax that we pay, and don’t let them write off losses that everybody knows are fake. Everybody knows that these losses are paper losses. The money’s being shipped out overseas. We know that, the Government knows that ... But they never touch them. It is time – all over the world – if the multinationals could be pulled into line because if they pay their share, everyone else will have to – we’ll all of a sudden find that everything’s down to a reasonable rate. I mean, these people deal in billions of dollars not in, you know, $50,000 a year or something like. They deal in billions of dollars.

Q: So you think the tax system generally is simply unfair?
A: It’s grossly unfair. The rich pay nothing.

Q: Grossly unfair?
A: Grossly unfair. It’s to the point of nearly being highway robbery. The middle and lower income earners are paying for everything. The rich at the top they don’t. They write it off on schemes. They can afford fancy accountants and all the rest of it. The rest of us can’t ... It’s ridiculous.

This subject was virtually alone in his charge that the tax system is distributively unfair.
Most business owners were less critical of the tax system overall and directed their criticism at the Tax Office specifically. They were mistrustful and cynical about it and its policies. A substantial proportion believe that little good and potentially a great deal of trouble and lost production time can come from contacts with the Tax Office. One remarked:

Q: How often does ATO come up – I realise these are unusual times because of GST coming in, right – but if you can go back to six months ago, before everyone started to worry about GST, how often does ATO come up in conversation on the job?
A: Hardly ever ...
Q: When it does come up, what is the general tenor of comments about the ATO?
A: Fear ... Probably it’s the fear of the unknown, you know. We all reckon that public servants are arrogant pricks anyway that really don’t know what they’re doing, and the only reason they’re there is because they couldn’t make it in the real world ... That’s the sort of attitude because when – if you talk to anybody that’s met them, that’s how they come over. It’s like a policeman standing there ... and everybody fears a policeman, don’t they? Doesn’t matter whether you’re not doing anything or whether you were, you know ... [Y]ou think, ‘what have I done wrong?’ And you get the same sort of thing when they mention the ATO or the Tax Department. ‘What in the hell have I done wrong now?’ And that’s the reason – they’re not there to help you, they’re there to nail you.

Another and unusually clear representation of this was given by a plumber who was interviewed, along with his business partner and mate on their job site:

I mean, it’s all too hard: that something that should be so simple is made so hard. On top of going to work and making a living, we’re expected to work all our tax out and everything else out, and it’s that bloody complicated. Chartered accountants can’t work it out who are trained to do that. And yet they want us to do it. I mean, like, how many of those guys can come and put up gutters and dig trenches and lay plumbing? Fucking none of them! But they expect us to be able to do – to keep our books in – in absolute perfect order.

The Tax Office is very inflexible when it comes to listening to any reasons why – it’s not like dealing with anybody else. I mean, it’s basically, ‘You were due to pay that on the 21st.’ And this one young lady ... I spoke to her and I said, ‘Look, you know, can I have, you know, two weeks [to meet tax obligations]?’ (And I had never defaulted on my taxes.) She said, ‘No, I’ve got a record here that you paid late the last two months.’ And I said, ‘Yes, but I have paid, and I am finding it really hard at the moment.’ She said, ‘No, you will pay like immediately or I’ll start fining you tomorrow, and you’re going to get’ – I can’t remember what she said – some sort of record as a problem payer ... And I thought she was a very hard woman ... So ... yes, I lost it. I
couldn’t even talk to her. I hung up. Anyway, she rang me back a couple of days later, and she was a little bit nicer. But ... it had got to the point where [our business] was really struggling.
Q: What is your impression of how small business owners like yourself generally see the ATO?
A: How do we see it?
Q: Yes. Does this ever come up in conversation between you and your mates?
A: Not really, no. The consensus is everybody hates it, you know. The Tax Office is there to rob us of any chance of making any profit for anything, and that’s it, and I think that’s the consensus with most people.

Another subject commented simply that ‘the public perceives them to be just a bully’.

Wariness and cynicism were not universal, however; a minority of the respondents noted that the Tax Office merely carries out policies enacted and modified periodically by ‘politicians’ (that is, Parliament). Consequently, a subject told us:

[I]f you need any advice, then who better to go to than the ATO – apart from your own accountant. [If] there are some little things that you might want to know ... the ATO will be able to tell you. So it’s best to go there.

One of the principal objectives of the ATO Compliance Model is improved business perception of the Tax Office and a more cooperative culture among business owners. No one expects this will be accomplished quickly, but the model rests on an assumption that over the long haul its use will produce effects of this type. Our interviews focused principally on subjects’ experiences with and perceptions of the Tax Office over the past five years. Few of the building and construction owners were aware that the Tax Office had launched the ATO Compliance Model, but a much larger number reported they had personal contacts with the Tax Office during this time. One of the most striking characteristics of the responses we received was the large proportion who spoke positively of the way they were treated in these contacts.5 A man whose business records were audited by Tax Office staff some 10 years ago commented on the contrast between that experience and a real time review conducted by the Tax Office approximately one year before our conversation:

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5 The one building and construction industry representative we interviewed was quite positive in his comments about responsive regulation as he had experienced it. He was impressed particularly by the willingness of Tax Office personnel to attend meetings of their organisation, to do presentations as part of the meeting program, and afterwards to answer questions posed by builders in attendance.
Q: You mentioned a few minutes ago that, historically, the building and construction industry is one where – you didn’t say it this way, but I think this is what you meant – people are suspicious of, a bit wary, of the Australian Taxation Office?
A: Years ago, yes ... Up until the last few years, you know. I must admit the first time I ever got audited that they treated me like a common criminal, you know, until you’re proven innocent. And consequently I had a shocking attitude to the Taxation Department because I just thought all they were trying to do is put you out of business ... I must admit I had a shocking attitude towards them ... But I think that the people that have contact with them now understand that they’ve got their job to do and that they are trying to be user friendly as much as possible ... I must admit, my attitude’s been changed completely.

As impressive as these comments are, they and others like them are subject to a host of interpretations other than the tempting one that business owners are changing their perceptions as a result of the Tax Office’s use of the ATO Compliance Model. The respondent was asked, for example:

Q: Do you think getting a little bit older also has anything to do with this?
A: Most certainly. Most certainly.
Q: How would you interpret that?
A: I just think that when you’re younger you’re a little bit more gung ho sort of thing ... but I think as you get older you start to become a little bit wiser and start to understand, you know, they’ve [ATO] got their job to do and, consequently, we need to pay taxes to have all the benefits that everybody needs. You do have that [attitude] ... when you’re young. And that’s when most companies are starting – they just want to go full on trying to get their businesses up and running, and if anybody comes in – it doesn’t matter if it’s the Taxation Department or anybody else – to interrupt what they’re trying to achieve then they would try to dismiss them ... And I think most people that run their businesses are inclined that way ... They just don’t like to be pulled up ... They just want to go for it.

Our cautious interpretation of what we were told, however, should not obscure the fact that this respondent was not alone in noting that he has seen a change in the Tax Office. Responding to a question, another business owner commented:

Q: Has this [most recent] contact [with ATO] in any way changed the way you think about them?
A: Absolutely. Absolutely. Like I said ... it was, first of all it was nice to see that it was actually a human being that worked for the Tax Office. Because as far as I always thought, they weren’t humans anyway. Yes, it was nice to have somebody you could look at and actually speak to, and, yes, he was a nice guy.
Q: But when we began talking, you used some of the words that [others] have used to describe them: ‘rude’, ‘arrogant’...
A: That’s right. Yes. And that was from speaking over the phone [with them]. And ... when I had this meeting with them some time ago, that was exactly the way that I’d always thought of them. Especially from that initial time [several years previously]. Yes, my perception definitely changed after having this guy here a couple of weeks ago. Like I said, he was nice, he was understanding. He explained, you know, what we wanted to know ... It was good to be one on one and see one of these guys.

It is well to recall again that the sample of firm owners we interviewed was made up almost entirely of those with a record of compliance. This should temper our readiness to interpret these findings as indicative of success for the ATO Compliance Model. They are strongly suggestive, however.

Lessons

Our research began with two overarching questions: (1) to what extent did the Tax Office have or acquire during the initial two years of operation of its CE/B&E project capacity to implement the ATO Compliance Model with a reasonable chance of success, and (2) what can be learned from the CE/B&C project initiative that could be useful now that the ATO Compliance Model has been extended throughout the Tax Office?

Regarding the former, there is strong evidence that Tax Office executives supported the ATO Compliance Model and provided adequate resources for its trial implementation. There is evidence also, albeit considerably weaker, that field-level staff gradually warmed to the approach although they continue to harbour ambivalence about it and reservations about its long-term impact. The ATO Compliance Model was adopted by the Tax Office during a time of considerable external change and uncertainty, and it can be extremely difficult to isolate and determine the effects of new policies under such conditions. The Tax Office was powerless to maintain an environment in which the CE/B&C project could function smoothly and reflectively. The problems, however, are not confined to the absence of stable environmental conditions; the ATO Compliance Model was adopted at a time of change and uncertainty within the Tax Office as well. Management initiatives to increase employee productivity, coupled with changes in employee work routines, contributed to pervasive uncertainty and stress.
For reasons presumably diverse and complex, some conditions important for achievement of reform initiatives did not materialise. Plans for evaluating the CE/B&C project were not built in and were hampered by shortcomings in routine data collection and management capabilities. The Tax Office’s Case Management Reports and Analysis system is a case in point. This system was designed for reporting in the area of withholding tax, and only later was modified for use in other tax areas. The modifications, however, were stopgap in nature, and the finished product was unsatisfactory. When applied to the CE/B&C project, the resulting system of data and case management was of limited use both for Tax Office personnel and for those who would use it to examine the implementation and effectiveness of the ATO Compliance Model. It proved unreliable as a guide for drawing our sample of firms with variable intensity of contact with the Tax Office during the preceding two years, and even efforts to determine how many real time reviews were conducted during the same period yielded inconsistent numbers. Despite indications of considerable organisational capacity for responsive regulation, the Tax Office probably will not know with any degree of confidence how well the program operated.

What lessons can be drawn from the CE/B&C project that may be of value now that the Tax Office has extended the ATO Compliance Model to all areas of compliance assurance? Clearly, new policies and procedures for evaluating them should be launched at one and the same time. This was not done when the Tax Office moved to responsive regulation of the small building and construction industry. One possible consequence of this is limited gain in knowledge of how to implement new policies and make them work soundly. An interview subject told us:

I think the biggest problem in the office is that we always go – we don’t have balance. We go all or nothing. So, we go compliance model ... ‘This is the be all and the end all, and it’s happening today, and everybody will live and breathe it.’ And that was the message that was put out: ‘You will live the compliance model’ ... It should be – and I am not sure how to achieve it – a more subtle thing; it should be built, and it shouldn’t just be bang, thrown on the table and ‘here, take it away. This is what you have got to do.’ We do a lot of things that way. The office seems to always work that way; if it is going to start something it doesn’t pilot it, it doesn’t test it, it goes for it.
Although this subject may be unaware of it, his comments on the importance of testing new programs carefully and rigorously are disputed by few policy analysts. Not only should they be tested, but procedures for doing so and a clear understanding of the specific kinds of data to be collected should be built into the program from the outset. Decisions about the kinds of evidence that will be taken as a sign of success or failure should be reflected in routine record keeping. Whether or not the turbulent environmental conditions in which the Tax Office has operated in recent years and its own unsettled internal worlds would have made possible anything more than was done is unknown, but Tax Office evaluation studies and the results of this research are cause for modest optimism.
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