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Working Paper No. 2005 - 30

CREMA Gellertstrasse 24 CH - 4052 Basel www.crema-research.ch

TAX MORALE AND FISCAL POLICY

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Abstract: Tax morale has received a growing attention in academics as well as in public life. The relevance of tax morale for fiscal policy cannot be neglected as tax morale can help to explain the level of tax compliance or tax evasion. This paper gives an overview of tax morale with a special focus on Switzerland. We highlight the magnitude and the determinants of tax morale that have been isolated so far and discuss directions for future research in this area. In particular, we concentrate on fiscal policy implications.

JEL classification: H260, 9160

Keywords: tax morale, tax compliance, tax evasion, fiscal policy

The unreasonable severity of the laws obstructs their execution
Montesquieu, 1748

I. INTRODUCTION

Taxation has ever been an important policy field throughout history and will stay a crucial aspect in future politics since it creates the basis for the state to work. However, despite the fact that a voluminous literature on taxation is available, some issues have rarely been studied. For example, research on the willingness to pay taxes is still rather underdeveloped. This paper is therefore designed to provide an overview of the tax morale research with a focus on the fiscal policy consequences.

Why is it important to analyze tax morale? The reasons of tax compliance and noncompliance have obtained increased attention in the last few years. It can be supposed that nobody likes paying taxes even though everybody knows that taxes are essential to the government. One possibility is to "enforce" citizens to pay taxes with a deterrence policy. However, conducting a universal enforcement strategy is connected with high costs and cannot be achieved unless there is a tax administrator under every bed. Slemrod (1992), for example states: "From the tax collection standpoint, it is extraordinarily expensive to arrange an enforcement regime so that, from a strict cost-benefit calculus, noncompliance does not appear attractive to many citizens. It follows that methods that reinforce and encourage taxpayers' devotion to their responsibilities as citizens play an important role in the tax collection process (p. 7)". Furthermore, several previous studies have shown the limitations of enforcement strategies (Graetz and Wilde 1985, Alm, McClelland and Schulze 1992, Frey and Feld 2002).

Thus, the question arises whether there are alternative strategies that help to increase tax compliance. Many researchers have stressed that tax morale, seen as the intrinsic motivation to pay taxes, is a key instrument that helps to explain tax compliance. Tax morale itself has in turn many facets, which are influenced by a variety of aspects. First, there is a cultural aspect. This implies that socio-demographic and socio-economic factors as well as national pride or religiosity play a role in determining tax morale in a society. Second, there is the institutional arrangement in which the government works. Here, the extent of democratic participation (possibilities) by taxpayers as well as the degree of decentralized taxation and the level of institutional trust are decisive. Third, there is a policy and administration aspect. For example, the behavior of the tax administration and the (perceived) tax burden, the tax struc-

ture in general as well as the tax enforcement strategy can affect individuals' willingness to pay taxes.

The reminder of the paper is as follows: In Section II we place the question of tax morale in the context of fiscal policy. Then, we present an overview of the tax morale literature in Section III and discuss the magnitude, the impact and the determinants of tax morale followed by Section IV pointing to future research needs that help to develop promising tax policy strategies. Finally, Section V provides some concluding remarks.

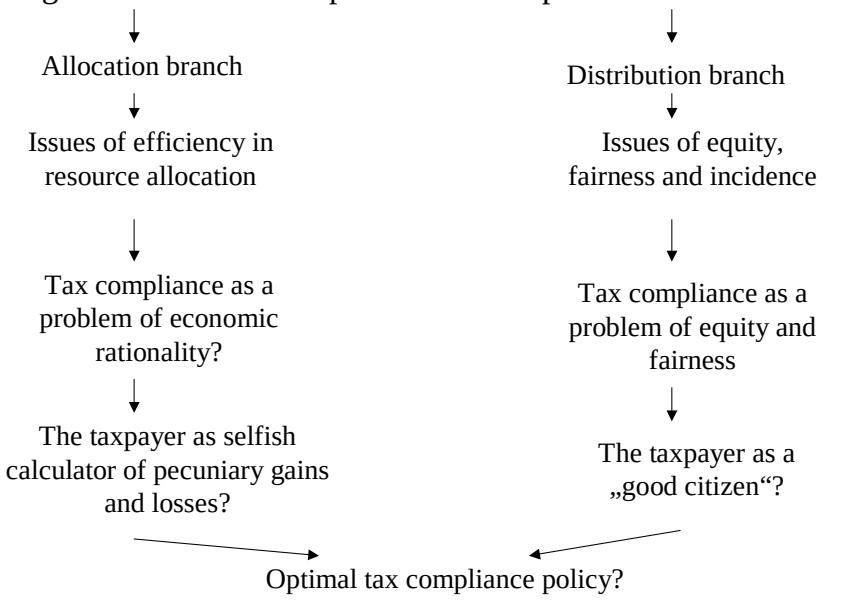
II. TAX MORALE IN THE CONTEXT OF FISCAL POLICY

Often, the view of tax compliance is based on a simplistic view of a law enforcement problem. However, tax evasion is not only an illegal activity but has also a lot to do with fiscal policy decisions by the government, the behavior of tax officials and cultural aspects. The effects of the tax system, the spending of tax revenues, the effectiveness of the administration, its behavior towards taxpayers and the size of the (perceived) tax burden have to be considered to get a more comprehensive picture on the question why people pay taxes. Thus, there are other instruments to be taken into account. Not only the level of tax compliance but also the level of tax morale is crucial to understand citizens' behavior. It is useful to take a closer look at what determines tax morale per se rather than treating it as a black box.

Tax morale is connected to the (economic) justification of taxation. It is decisive how the government taxes the economy and how the government spends the revenues. Musgrave (1959) considered three requirements of fiscal policy: the allocation, the distribution and the stabilization aspect. In the context of tax morale, the first two aspects are especially of interest. While the allocation branch influences tax morale by an efficient allocation of resources, the distribution aspect touches equity and incidence considerations, which have an impact on tax morale, too. In the first case, the tax compliance calculus is based on an individual cost-benefit analysis of expected pecuniary gains and losses from compliance and non-compliance. In the second case, the taxpayer is more than a simple mechanical calculator but a member of the society considering different aspects when paying taxes including equity, fairness and incidence. *Figure 1* developed by James, Hasseldine, Hite and Toumi (2001) illustrates the two approaches to tax compliance. Tax morale touches both branches. The allocation branch is important because the spending in the sense of tax revenue allocation affects morale considerations. The distribution branch is important because fairness considerations are strongly

related to (tax) morale beliefs. Thus, an optimal tax morale or tax compliance strategy is based on efficiency as well as equity measures.

Figure 1: Rationale for public sector expenditure and taxation



Source: James et al. (2001)

III. TAX MORALE: MAGNITUDE AND DETERMINANTS

Tax morale is closely linked to tax evasion. A major difficulty in analyzing tax evasion lays in its measurement. After all, individuals have incentives to conceal their cheating. Several methods have been developed to measure evasion. Even though they are all subject to imprecision and controversy, in sum they give a good picture of the dimension of tax evasion.

One method involves surveys. These surveys are typically designed to elicit taxpayers' attitudes about their reporting, but such surveys can also be used to estimate non-compliance. A main advantage is that they include many socio-economic, demographic and attitudinal variables. This helps to investigate and test a rich set of (new) theories. Furthermore, surveys help to compare different countries and to get insights into the development over time. In the last years, economists have increasingly focused on surveys (see, for example, the happiness research done by Frey and Stutzer 2002). One reason might be that survey research uses more sophisticated statistical techniques and designs compared to some years ago. Certainly, the accuracy of surveys is not fully clear. Individuals may not remember their reporting decisions, they may not respond truthfully or the respondents may not be representative as the sensitive

nature of compliance information might create the incentive not to participate in such a survey.

Another direct method relies on information generated by the tax authority as part of its audit process. The Internal Revenue Service (IRS) conducts line-by-line audits of individual tax returns for its Taxpayer Compliance Measurement Program (TCMP). These audits yield an estimate of the taxpayer's "true" income, allowing measures of individual and aggregate tax evasion to be calculated. However, TCMP data have some serious deficiencies: The audits do not detect all underreported income, non-filers are not often caught, ‘honest errors’ are not identified, and final audit adjustments are not included.

Indirect methods attempt to infer the magnitude of unreported income from its traces in other, observable areas. One approach looks at discrepancies between income and expenditures in budget surveys and in national income accounts. Another approach looks at discrepancies between "official" labor force participation rates and estimates of "true" participation rates. A third approach looks for traces of unreported income in monetary aggregates. All of these methods are subject to serious criticism. They may simply compound measurement errors, they attribute all discrepancies to unreported income, and often they are only able to estimate the change in unreported income over some period, not its absolute level. However, especially the last method has gained much attention in the literature. Unfortunately, compliance and enforcement data are difficult to obtain, if they exist at all. For example, most reliable estimates by the IRS suggest a tax gap of the federal income tax of some US-$ 257-298 billion in 2001, which equals a non-compliance rate of about 15.5% to 16.6% for the federal income tax (IRS, 2005). For Switzerland, Feld and Frey (2002) estimate an average tax gap of 23.5% of all income tax for the years 1970 to 1995.

Using (laboratory) experiments is a further approach. They allow circumventing the problem of getting honest answers on illegal behavior. Researchers can use own data obtained from experiments. The strength of this approach is the possibility to control for and manipulate the variables of interest. This allows reducing causality problems and thus gives good information not only about the relationship between two variables but also about the direction of the effect (for a detailed discussion see Torgler 2002).

1. Magnitude

Similar to one measurement approach on tax evasion, a possibility to evaluate the magnitude of tax morale is via surveys. The World Values Survey provides a valuable data source for

getting internationally comparable information on tax morale. Switzerland provides a natural laboratory for analyzing the institutional and cultural impact on tax compliance and tax morale. The country has participated in 1988/89 and 1996. To assess the level of tax morale in the World Values Survey we use the following question:

> "Please tell me for each of the following statements whether you think it can always be justified, never be justified, or something in between: … Cheating on tax if you have the chance". The question leads to a ten scale index of tax morale with the two extreme points "never justified" and "always justified".

The ten-point scale has been recoded into a four-point scale (0,1,2,3), with the value 3 for "never justifiable". 4-10 have been integrated in the value 0 due to a lack of variance. *Table 1* provides a comparison of Switzerland's tax morale levels to those of 20 other OECD countries. This allows comparing the development in Switzerland in relation to other countries. The descriptive analysis reveals the percentage of individuals in each OECD country stating that 'tax evasion is never justifiable' (i.e., those with the highest level of tax morale) and the mean level of tax morale among OECD countries.

First, *Table 1* shows that in 1988/89 the average number of people in Switzerland stating that tax evasion is never justified was 63.8%, which was far above the OECD average of 54.5%. This value decreased to not less than 53.5% (below the average of 60%). Further the average score obtained for the tax morale question across all OECD countries in 1988/89 was 2.08 (OECD average 1.94) (out of 3) compared to 1.95 in 1996 (OECD average 2.12). However, a full comparison is limited due to a lower number of OECD countries that participated in the 1995-1997 surveys. The high level of tax morale in Switzerland for the year 1988/89 is supported in a multivariate analysis controlling for additional factors working with 16 OECD countries (see Alm and Torgler 2005).

To get a better idea of what is behind the different tax morale scales, in *Figure 2* we present a histogram with the distribution of tax morale scores in each of the two different years. The results indicate large differences between the percentage of individuals with a high tax morale (a score of 3); on the other hand the distributions for the lowest score values is quite stable. The deterioration in tax morale in Switzerland from 1988/89 to 1996 was strongly affected by a reduction in the share of those citizens who believe that tax evasion is never justifiable (the score of 3). Further evidence on the nature of these changes is presented in *Table 2*, which tests whether the different samples have the same distribution using the Wilcoxon rank-sum (Mann-Whitney) test. The results indicate that there is a significant dif-

ference between 1988/89 and 1996. Tax morale decreased in a statistically significant manner over time between 1988/89 and 1996. The result requires a careful investigation whether such a trend remained consistent between 1996 and 2005. If this is the case, further questions are how to explain such a decay in tax morale over time and how to develop policy strategies that help to improve tax morale in Switzerland.

Table 1: Tax morale levels among OECD Countries over Time

Country	Year	Percentage of respondents stating tax evasion is never justified	Mean score on tax morale question	Year	Percentage of respondents stating tax evasion is never justified	Mean score on tax morale question
Austria	1990	62.3	2.26			
Australia				1995	62.1	2.18
Belgium	1990	33.9	1.28			
Canada	1990	59.2	2.08			
Denmark	1990	57.3	2.03			
Finland	1990	40.3	1.64	1996	57.4	2.01
France	1990	46.5	1.69			
Germany*	1990	53.8	2.00	1997	46.9	1.76
Great Britain	1990	53.9	1.94			
Iceland	1990	56	2.00			
Ireland	1990	48.8	1.80			
Italy	1990	69.7	1.97			
Northern Ireland	1990	55.2	2.25			
Japan	1990	81.9	2.64	1995	80.6	2.62
Netherlands	1990	42.9	1.66			
Norway	1990	43.1	1.64	1996	47.5	1.83
Portugal	1990	39.9	1.46			
Spain	1990	58.4	1.96	1995	69.5	2.33
Sweden	1990	56.4	2.01	1996	49.3	1.87
Switzerland	1988-1989	63.8	2.08	1996	53.5	1.95
USA	1990	66.7	2.31	1995	73.6	2.48
Average		**54.5**	**1.94**		**60.0**	**2.12**

Notes: * The 1981 value of Germany considers only West Germany.

Figure 2: Tax Morale Distribution over Time in Switzerland

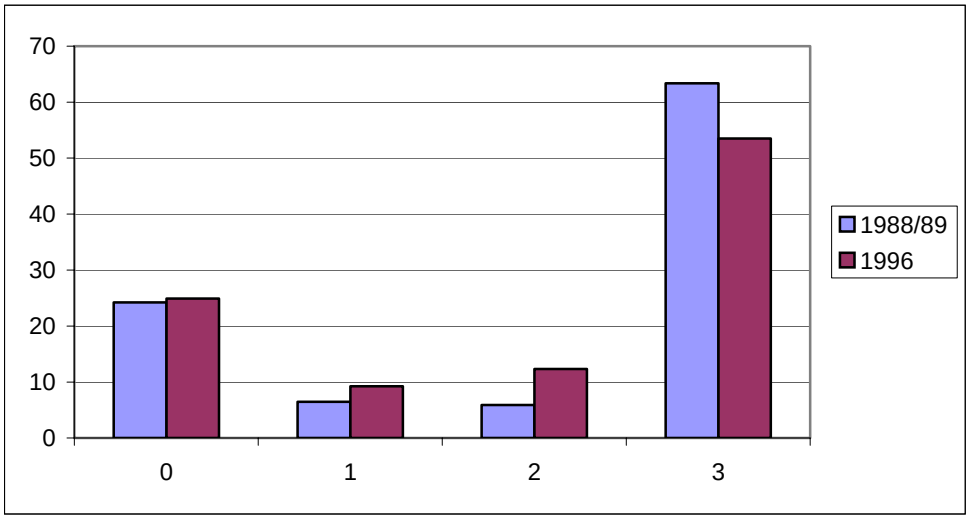


Table 2: Two-Sample Wilcoxon Rank-Sum (Mann-Whitney) Test

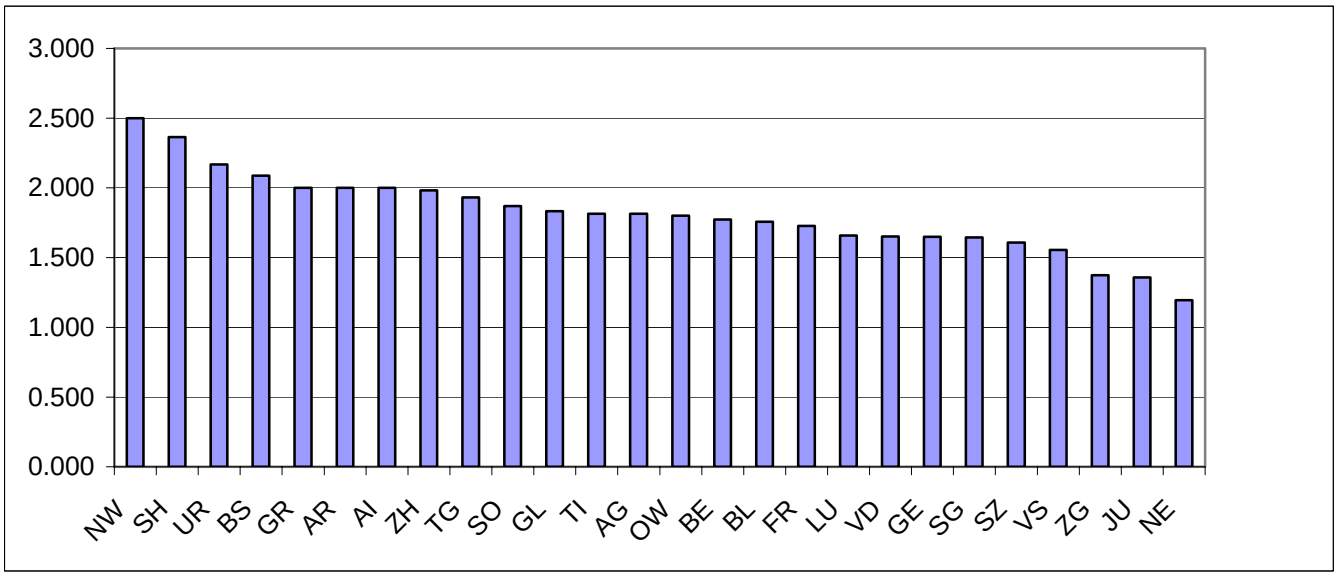
Hypothesis	**z-value**	**Prob > |z|**
H_0: Tax Morale Switzerland 1988/89 = Tax Morale Switzerland 1996	3.685	0.0002

Another possibility to measure tax morale is via the International Social Survey Programme (ISSP). The *International Social Survey Programme (ISSP)* cross-national collaboration started in 1983 and has grown to more than 30 nations (mostly European countries) and brings together different kinds of social science projects. We will analyze the data set RELIGION II (ISSP 1998). The following question was asked:

> "Do you feel it is wrong or not wrong if a taxpayer does not report all of his or her income in order to pay less income taxes? (1= not wrong, 2= a bit wrong, 3= wrong, 4=seriously wrong)".

The ISSP is interesting as it allows investigating the most recent available data set on tax morale for Switzerland (data 1999). *Figure 3* presents the mean values in the cantons, calculated as the simple average across all individuals in every canton. As we can see there are strong differences among cantons, with the highest tax morale. A high level of tax morale is observed in the cantons of NW, SH, UR and BS. On the other hand, the lowest values are found in VS, ZG, JU and NE. Certainly, due to the low number of observations at the cantonal level (total sample size covers only 1283 observations), results should be treated with caution.

Figure 3: Tax Morale in Swiss Cantons (ISSP 1999)



In a next step we compare the Swiss data for 1999 with other countries presenting in *Table 3a* a cross-tabulation of all tax morale scales among OECD countries and reporting in *Table 3b* the mean values for these country sorted by the level of tax morale. The results are similar to the ones obtained with the World Values Survey 1995-1997. Switzerland is below the average value classified in place 14 out 18 countries (counting both German regions together). *Table 3a* shows that a relatively low amount of individuals stated that tax evasion is *seriously wrong*. However, a relatively high amount of individuals stated that tax evasion is *wrong*. On the other hand, the percentage of individuals stating that tax evasion is *not wrong* is also in comparison to other countries quite high (fifth highest). Consistent in both surveys is the relatively high tax morale in Japan, the USA, Australia, Denmark and Spain. Furthermore, consistent is also the relatively low tax morale in France, Ireland, Germany and Netherlands. On the other hand, strong differences are observed for Austria.

In sum, the results for tax morale show that Switzerland ranks in the lower midfield, while there is a trend towards declining tax morale over time (for a discussion of possible reasons, see Kirchgässner 2005). This applies for Switzerland as a whole. Interestingly, there are strong differences for tax morale within Switzerland.

Table 3a: ISSP Tax Morale Values, 1999

Country		Tax Morale				Total
		1	2	3	4	
Australia	Count	24	166	620	418	1228
	% within Country	2.00%	13.50%	50.50%	34.00%	100.00%
Germany-West	Count	138	305	292	185	920
	% within Country	15.00%	33.20%	31.70%	20.10%	100.00%
Germany-East	Count	109	246	333	239	927
	% within Country	11.80%	26.50%	35.90%	25.80%	100.00%
Great Britain	Count	18	186	423	151	778
	% within Country	2.30%	23.90%	54.40%	19.40%	100.00%
Northern Ireland	Count	53	176	365	163	757
	% within Country	7.00%	23.20%	48.20%	21.50%	100.00%
United States	Count	57	127	624	384	1192
	% within Country	4.80%	10.70%	52.30%	32.20%	100.00%
Austria	Count	176	316	292	170	954
	% within Country	18.40%	33.10%	30.60%	17.80%	100.00%
Italy	Count	117	185	270	412	984
	% within Country	11.90%	18.80%	27.40%	41.90%	100.00%
Ireland	Count	105	282	377	216	980
	% within Country	10.70%	28.80%	38.50%	22.00%	100.00%
Netherlands	Count	45	723	735	481	1984
	% within Country	2.30%	36.40%	37.00%	24.20%	100.00%
Norway	Count	72	290	680	464	1506
	% within Country	4.80%	19.30%	45.20%	30.80%	100.00%
Sweden	Count	35	177	496	457	1165
	% within Country	3.00%	15.20%	42.60%	39.20%	100.00%
Canada	Count	37	163	439	311	950
	% within Country	3.90%	17.20%	46.20%	32.70%	100.00%
Japan	Count	27	170	343	699	1239
	% within Country	2.20%	13.70%	27.70%	56.40%	100.00%
Spain	Count	145	318	559	1377	2399
	% within Country	6.00%	13.30%	23.30%	57.40%	100.00%
France	Count	113	344	366	273	1096
	% within Country	10.30%	31.40%	33.40%	24.90%	100.00%
Portugal	Count	76	168	564	379	1187
	% within Country	6.40%	14.20%	47.50%	31.90%	100.00%
Denmark	Count	55	216	350	484	1105
	% within Country	5.00%	19.50%	31.70%	43.80%	100.00%
Switzerland	**Count**	**126**	**266**	**499**	**252**	**1143**
	% within Country	**11.00%**	**23.30%**	**43.70%**	**22.00%**	**100.00%**

Table 3b: ISSP Mean Tax Morale Values

Country	Mean	Std. Deviation
Austria	2.478	0.988
Germany-West	2.570	0.974
Ireland	2.718	0.926
France	2.729	0.950
Germany-East	2.757	0.967
Switzerland	2.767	0.917
Netherlands	2.833	0.818
Northern Ireland	2.843	0.839
Great Britain	2.909	0.720
Italy	2.993	1.041
Norway	3.020	0.832
Portugal	3.050	0.846
Canada	3.078	0.806
United States	3.120	0.779
Denmark	3.143	0.902
Australia	3.166	0.726
Sweden	3.180	0.795
Spain	3.321	0.920
Japan	3.383	0.801
Average	2.950	0.871

2. Determinants

After having discussed the magnitude of tax morale in OECD countries, the question of the determinants of tax morale arises. First important findings in the tax compliance literature date from the 60s and 70s by German scholars around Günter Schmölders (1951/1952, 1960, 1962, 1970) known as the 'Cologne school of tax psychology'. They have emphasized that economic phenomena should not only be analyzed from the traditional point of view. They saw tax morale as an attitude regarding tax (non-) compliance (see, e.g., Schmölders 1960). In their surveys they used the subjective tax burden as an indicator for the level of tax morale and found that self-employed people reveal lower tax morale than employees. Strümpel (1969), for example, analyzed tax morale and the tax systems on the basis of a European-wide comparative survey. He points out that treating taxpayers with great caution helps cultivating tax morale and reducing tax compliance costs.

In the last 15 years, the main research interest was to discover the reasons why people pay taxes? At a first glance, this may sound as an unorthodox research question. However,

taking in account that many people pay their taxes although fines and audit probability are low, the question is not only reasonable but also crucial for the design of an efficient tax system (see, e.g., Erard and Feinstein 1994). In an overview Andreoni, Erard and Feinstein (1998) point out that "adding moral and social dynamics to models of tax compliance is as yet a largely undeveloped area of research" (p. 852). Important questions arise out of this research. Are there taxpayers who are always honest and don't search for ways to cheat at taxes, independently of the regime? If yes, what is the percentage of these individuals? Are there individuals who are inclined to dodge their taxes but are not able to translate this intention into actions? How is it possible to guarantee that honest taxpayers remain compliant? What possibilities are available to bring tax evaders back on the routes of honesty?

In the next section we present an overview of the results obtained in the tax morale literature (Torgler 2006a[1]). The results can be seen as an attempt to extend the traditional neoclassic assumption, enriching theory with conceptions from other sciences as psychology without losing the economic foundation and testing them empirically. A neutral concept of taxpayers' utility or preferences is considered, which includes different sorts of human motivation. Such a basis allows for a multi-faceted approach, which goes beyond traditional theories of enforcement strategies to understand why individuals pay taxes.

2.1 Socio-Demographic and Socio-Economic Variables

Socio-demographic factors appear to be important determinants of behavior, also when it comes to tax morale. *Table 4* to *6* indicate the sign of the coefficient values of the different groups compared to the reference group and whether the effect is statistically significant.[2]

We first start with the variables *age, gender, and education*. Most theories regarding the effects of socio-demographic factors on compliance behavior have been developed by social psychologists. Tittle (1980) argues, for example, that elderly people are more sensitive to the threats of sanctions. They have acquired greater social stakes over the years as property or social status, and thus show a stronger dependency on the reactions from others, so that the potential costs of sanction increase. The results in *Table 4* to *6* underline the effect of the age variables. In most estimates age is significantly and positively correlated with tax morale or tax compliance.

[1] For detailed studies see also Torgler (2003b, 2003c, 2003d, 2003e, 2003f, 2003g, 2004a, 2004b, 2004c, 2005a, 2005b, 2006b).

[2] In some studies, mostly experiments, age has been coded as continuous variable. Similarly, gender has been coded as dummy variable (being male in the reference group).

Similarly, research in social psychology suggests that gender matters: females are more compliant and less self-reliant than males (e.g., Tittle 1980). According to Tittle the reason is based on the traditional role of women in society. However, if this is correct, today's female generation, which is much more independent than the former generations, should comply less. Another possibility could be that females are more risk averse than males. The results reported in *Table 4* to *6* cannot find support for the first reason. Though females report significantly higher tax morale than males in many cases, there is no difference between developing and developed countries.

Education is related to taxpayer's knowledge about the tax law. Well educated taxpayers are supposed to know more about the tax law and fiscal connections, they are aware of the benefits and services the state provides for the citizens from the revenues and thus are in a better position to assess the degree of compliance (see Lewis 1982). On the other hand, highly educated taxpayers should also be more aware of possible government wastes. Furthermore, they may be less compliant because they better understand the opportunities for evasion and avoidance and might be more critical about how the state uses tax revenues. Based on these opposing arguments, it is not surprising that the results show an ambivalent picture. In many estimates the effect of education on tax compliance is not statistically significant. In the estimates where the coefficient exhibits a significant influence the signs are also mixed. These results might indicate that the current politico-economic situation (government spending, the input-output relation between paid taxes and obtained benefits) influences the education variable.

Table 4: The Effects of Age, Gender and Education on Tax Morale and Tax Compliance in Europe

Dependent Variables:	**Sign and Significance of the Coefficient**					
Tax Compliance and Tax Morale	Age (dummies compared to age 16-29)			Age	Gender	Education
Countries	AGE 30-49	AGE 50-64	AGE 65+		FEMALE	
COUNTRIES POOLED						
Europe 1989-1990 (WVS)	+	+	+		+	
SPECIFIC COUNTRIES						
Switzerland						
1989 (WVS)	+	+	+		+	(-)
1996 (WVS)	(+)	+	(+)		+	(+)
1999 (ISSP)	(±)	(±)	(±)		(±)	+
Experiment (Public Good)				+	(+)	
Experiment (Public Good)				-	+	+
Experiment (Tax Amnesty)				+	+	
Field Experiment	(+)	(+)	+		+/(-)*	
Germany						
West Germany 1997 (WVS)	(-)	(+)	(+)		(+)	-
East Germany 1997 (WVS)	+	+	+		(+)	-
W. Germany 90 and 97 (pooled)	(-)	+	+		+	
E. Germany 90 and 97 (pooled)	+	+	+		+	
Spain						
1990 (WVS)	+	+	+		(+)	+
1995 (WVS)	(-)	(±)	(±)		+	(-)
Belgium						
1990 (WVS)	+	+	+		+	(±)
Great Britain	(+)	+	+		(+)	(±)
1990 (WVS)						

Notes: In the surveys the dependent variable is tax morale, in the experiments tax compliance. Gender: reference group MALE. +: significant positive coefficient, (+), (-), positive, respectively negative coefficient sign without being significant, (±) positive and negative sign of the coefficient without being significant. * Females have a higher compliance regarding timely paying the taxes than couples, on the other hand regarding the timely filling out there is a lower compliance, but without being significant.

Table 5: The Effects of Age, Gender and Education on Tax Morale and Tax Compliance in North and Latin America

Dependent Variables:	**Sign and Significance of the Coefficient**					
Tax Compliance and Tax Morale	Age (dummies compared to age 16-29)			Age	Gender	Education
Countries	AGE 30-49	AGE 50-64	AGE 65+		FEMALE	
COUNTRIES POOLED						
Latin America (WVS 1995-1997)	+	+	+		+	(-)
Latin America (Latinobarómetro 1998)	+	+	+		(+)	(+)
SPECIFIC COUNTRIES						
USA						
1995 (WVS)	(+)	(+)	(+)		+	(+)
1987 (Taxpayer Opinion Survey)				+	(±)	-
Canada						
1990 (WVS)	+	+	(+)		+	(+)
Costa Rica						
1998 (Latinobarómetro)	(+)	(+)	+		(±)	
Experiment (Public Good)*				+	+	+
Experiment (Alternative Tax Policy Strategies)				(+)	+	+

Notes: In the surveys the dependent variable is tax morale, in the experiments tax compliance. Gender: reference group MALE. +: significant positive coefficient, (+), (-), positive, respectively negative coefficient sign without being significant, (±) positive and negative sign of the coefficient without being significant. * only descriptive statistics.

Table 6: The Effects of Age, Gender and Education on Tax Morale and Tax Compliance in Transition and Asian Countries

Dependent Variable:	**Sign and Significance of the Coefficient**				
Tax Morale	Age (dummies compared to age 16-29)			Gender	Education
Countries	AGE 30-49	AGE 50-64	AGE 65+	FEMALE	
COUNTRIES POOLED					
Transition Countries (WVS 1989-1993)	+	+	+	+	
Transition Countries (WVS 1995-1998)	+	+	+	+	
Asia (WVS 1995-1997)	+	+	+	(+)	+
SPECIFIC COUNTRIES					
TRANSITION COUNTRIES					
Former Soviet Union Countries					
Russia 1991 and 1995 (pooled)	+	+	+	(±)	
Estonia 1990 and 1996 (pooled)	+	+	+	+	
Latvia 1990 and 1996 (pooled)	+	+	+	+	
Lithuania 1990 and 1996 (pooled)	+	+	+	+	
Belarus 1990 and 1996 (pooled)	+	+	+	(-)	
Central/Eastern Europe					
Poland 1989 and 1997 (pooled)	+	+	+	+	+
Bulgaria 1990 and 1997 (pooled)	+	+	+	(+)	
Slovenia 1992 and 1995 (pooled)	+	+	+	+	
ASIA					
India					
1995/1996	+	+	(+)	(+)	(+)
1990 and 1995/1996 (pooled)	+	+	-	+	+
Japan					
1995	+	+	(+)	(±)	
1981, 1990 and 1995 (pooled)	+	+	+	+	

Notes: Dependent variable: tax morale. Gender: reference group MALE. +: significant positive coefficient, (+), (-), positive, respectively negative coefficient sign without being significant, (±) positive and negative sign of the coefficient without being significant.

Second, we evaluate the effects of the *marital status, employment, economic situation and religiosity* on tax morale. Marital status might influence legal or illegal behavior depending on the extent to which individuals are constrained by their social networks (see Tittle 1980). On the one hand, such a constraint might have a positive impact on tax morale. It can be assumed that couples have more social stakes in their neighborhood and feel more committed to the social and political community where they live than singles. On the other hand, it should be noticed that this variable is interacting with the tax system. Differences in the degree of tax morale might be based on different tax treatments of married and non-married people (e.g. the so-called “marriage penalty”). However, evidence from Switzerland and the United States shows a tendency for married people to have stronger tax morale than singles, which would

not be in line with this argument. Such a tendency can be observed among different cultural settings, especially regarding the significant coefficient values.

Regarding the occupation status special attention has been paid to the question whether self-employed taxpayers have lower tax morale than full-time employees. *Tables 7* to *9* present the findings. In many equations the coefficient is not significant. However, it is interesting to notice that in the transition countries (see also East Germany) the coefficient is mostly significant with a negative sign. In these countries self-employed individuals might feel the financial restriction much more, as the compliance costs and taxes become more visible. The rapid collapse of institutional structures produced a vacuum in many countries, followed by large social costs, especially in terms of worsening income inequality and poverty rates and bad institutional conditions, based on uncertainty and high transaction costs.

The effects of income on tax morale are difficult to assess theoretically. Depending on risk preferences and the progression of the income tax schedules, income may increase or reduce tax morale. Looking at tax evasion it can be argued that in countries with a progressive income tax rate, taxpayers with a higher income realize a higher dollar return by evading, but with possibly less economic utility. On the other hand, lower income taxpayers might have lower society “stakes” or restrictions but are less in the position to take these risks, because of a high marginal utility loss (wealth reduction) if they are caught and penalized (Jackson and Milliron 1986). Thus, it does not surprise that the empirical findings show a mixed picture. Looking at the statistically significant coefficient, there is the tendency that higher income leads to lower tax morale. The positive results obtained in the experiments cannot be compared to the surveys, as not individual income has been integrated into the estimations, but the assigned income during the experiments.

Finally, *Table 7* to *9* present evidence regarding the variable religiosity, measured as church attendance and the perceived degree of religiosity. The results suggest a positive correlation between church attendance/religiosity and tax morale. According to Kirchgässner (2003), the religious affiliation might also play a role. While in the catholic tradition disputes between the church and the state authorities occurred regularly during medieval times and also later, in mainly protestant countries the church and the state had much closer ties. Thus, the religious affiliation could also be a determinant in the extent to which citizens feel committed to the financing of the state. This in turn might be a reason why we observe higher tax morale in Nordic countries compared to Roman countries.

Table 7: The Effects of Marital and Employment Status, Economic Situation and Religiosity on Tax Morale and Tax Compliance in Europe

Dependent Variables:	**Sign and Significance of the Coefficients**					
Tax Compliance and Tax Morale	Marital Status	Employm.	Economic Situation		Religiosity	
Countries	MARRIED	SELF-EMPL.	INCOME	F. SATISF.	CHURCH ATT.	RELIGIOUS
COUNTRIES POOLED						
Europe 1989-1990 (WVS)	+	-	-	+	+	
SPECIFIC COUNTRIES						
Switzerland						
1989 (WVS)	(±)	(-)	-	(+)	+	
1996 (WVS)	+	(+)	(+)	+	+	
1999 (ISSP)	(±)*		(+)		+	
Experiment (Public Good)			+			(+)
Experiment (Public Good)	+		(-)			(+)
Experiment (Tax Amnesty)				+	+	
Field Experiment	-	(+)	(+)			
Germany						
West Germany 1997 (WVS)	+	(-)	-	+	+	+
East Germany 1997 (WVS)	(+)	-	(-)			
W. Germany 90 and 97 (pooled)	+	(+)	-			
E. Germany 90 and 97 (pooled)	(+)	(-)	-			
Spain						
1990 (WVS)	+	-	-	+	+	
1995 (WVS)	(+)	(+)	(+)		(+)	
Belgium						
1990 (WVS)	+	-		+	+	
Great Britain						
1990 (WVS)	(+)	(-)	(+)	+	+	+

Notes: In the surveys the dependent variable is tax morale, in the experiments tax compliance. Marital status: reference group SINGLE, employment status: FULL TIME EMPLOYED. +: significant positive coefficient, (+), (-), positive, respectively negative coefficient sign without being significant, (±) positive and negative sign of the coefficient without being significant. *married and people living together are in one class.

Table 8. The Effects of Marital and Employment Status, Economic Situation and Religiosity on Tax Morale and Tax Compliance in North and Latin America

Dependent Variables:	**Sign and Significance of the Coefficients**					
Tax Compliance and Tax Morale	Marital Status	Employm.	Economic Situation		Religiosity	
Countries	MARRIED	SELF-EMPL.	INCOME	F. SATISF.	CHURCH ATT.	RELIGIOUS
COUNTRIES POOLED						
Latin America (WVS 1995-1997)	+	(+)	+	+		+
Latin America (Latinobarómetro 1998)	+*	(+)	(±)			
SPECIFIC COUNTRIES						
USA						
1995 (WVS)	+	(+)	-	+	+	+
1987 (Taxpayer Opinion Survey)	(-)		(-)			
Canada						
1990 (WVS)	+	(±)	-	+	+	+
Costa Rica						
1998 (Latinobarómetro)	(-)*	(+)	-			+
Experiment (Public Good)			+			+
Experiment (Alternative Tax Policy Strategies)**	+		-			+

Notes: In the surveys the dependent variable is tax morale, in the experiments tax compliance. Marital status: reference group SINGLE, employment status: FULL TIME EMPLOYED. +: significant positive coefficient, (+), (-), positive, respectively negative coefficient sign without being significant, (±) positive and negative sign of the coefficient without being significant. *married and people living together are in one class.** only descriptive statistics.

Table 9: The Effects of Marital and Employment Status, Economic Situation and Religiosity on Tax Morale in Transition and Asian Countries

Dependent Variable:	**Sign and Significance of the Coefficients**					
Tax Morale	Marital Status	Employm.	Economic Situation		Religiosity	
Countries	MARRIED	SELF-EMPL.	INCOME	F. SATISF.	CHURCH ATT.	RELIGIOUS
COUNTRIES POOLED						
Transition Countries (WVS 1989-1993)	+	-		+		
Transition Countries (WVS 1995-1998)	+	-		(+)		
Asia (WVS 1995-1997)	+	-		+		
SPECIFIC COUNTRIES						
TRANSITION COUNTRIES						
Former Soviet Union Countries						
Russia 1991 and 1995 (pooled)	(+)	-				
Estonia 1990 and 1996 (pooled)	(±)	-				
Latvia 1990 and 1996 (pooled)	(+)	-				
Lithuania 1990 and 1996 (pooled)	(+)	-				
Belarus 1990 and 1996 (pooled)	+	-				
Central/Eastern Europe						
Poland 1989 and 1997 (pooled)	(±)					
Bulgaria 1990 and 1997 (pooled)	(+)	(-)				
Slovenia 1992 and 1995 (pooled)	(+)	-				
ASIA						
India						
1995/1996	(+)	(-)	-			
1990 and 1995/1996 (pooled)	(+)	-	-			
Japan						
1995	-	-	(+)			-*
1981, 1990 and 1995 (pooled)	+	-	-		+	+**

Notes: Dependent variable: tax morale. Marital status: reference group SINGLE, employment status: FULL TIME EMPLOYED. +: significant positive coefficient, (+), (-), positive, respectively negative coefficient sign without being significant, (±) positive and negative sign of the coefficient without being significant. * Hindu compared to people without a religion denomination. **Buddhist compared to people without a religion denomination

2.2 Trust, Treatment of Taxpayer and National Pride

Not only the socio-demographic and the socio-economic background affect tax morale. Trust in government decisions and credibility of government action is also of importance. Trust is not an attitude that can be demanded by the government, taxpayers bestow trust on their government or they don't. However, governments can foster trust by an historic record eventually establishing a good reputation. In this context the willingness to pay taxes is highly influenced by the treatment of taxpayers by tax authorities. In order to collect tax revenue efficiently, tax officials are interested in keeping the costs of collecting taxes at a minimum. Respectful treat-

ment of taxpayers tends to support tax morale, which in turn considerably lowers the cost of tax collection. In contrast, a disrespectful treatment of taxpayers undermines tax morale consequently increasing the costs of raising taxes since the carrying out of audits becomes a rule rather than being the exception.

The crucial question in this context is: what is a respectful treatment of taxpayers? Empirical analyses show that two aspects are of importance (Frey 2003): First, transparency of procedures applied by the tax authority. In the case of arbitrary procedures and decisions taxpayers get the feeling of an unfair treatment and that they are not taken seriously. In contrast, if procedures are clearly and openly communicated and if the decisions by the state and the tax officials can be comprehended easily by taxpayers, the motivation to comply with the tax law is much higher. Second, taxpayers systematically respond to the personal treatment by public officials, government members and especially tax officials. If the treatment takes the form of partners in a psychological contract, taxpayers behave more honestly while being treated like an inferior in a hierarchical relationship violates intrinsic motivation to comply. At the same time this does not imply that deterrence activities do not play any role. In particular, deterrence has to be used against dishonest citizens to prevent honest taxpayers from being exploited. In general, the optimal balance between respectful treatment and deterrence has been achieved, where the system in place is able to distinguish between minor mistakes by taxpayers that should not be treated as criminal offenses and cheaters trying to fraud systematically the tax authorities.

In fact, an empirical study by Frey and Feld (2002) shows that the more respectfully tax administration treats taxpayers the higher tax compliance. In addition, they show that tax evasion is lowest in the case, where minor mistakes in the tax declarations are not treated as a delinquency in contrast to intentional tax fraud being punished severely (see also obtained results in *Table 14*).

Tables 10 to *12* show also the empirical evidence of a further variable: national pride. Taking into account that this variable has been completely neglected in the tax compliance literature, the evidence indicates that more attention should be paid to the effects of pride on tax morale and tax compliance. In almost all estimates a national pride leads to significantly stronger tax morale. Thus, independent of the cultural setting, this variable has a strong effect on tax morale.

Table 10: The Effects of Trust and National Pride on Tax Morale in Europe

Dependent Variable:	**Sign and Significance of the Coefficients**			
Tax Morale	TRUST			PRIDE
Countries	TRUST IN GOVERN.	TRUST LEGAL SYS.	TRUST IN COURT/LEG. S.	
COUNTRIES POOLED				
Europe 1989-1990 (WVS)		+		+
SPECIFIC COUNTRIES				
Switzerland				
1989 (WVS)				(+)
1996 (WVS)	+	+		
1999 (ISSP)			+	
Spain				
1990 (WVS)		+		+
1995 (WVS)	+	+		
Belgium				
1990 (WVS)		+		+

Notes: Dependent variable: tax morale. +: significant positive coefficient, (+), (-), positive, respectively negative coefficient sign without being significant, (±) positive and negative sign of the coefficient without being significant.

Table 11: The Effects of Trust and National Pride on Tax Morale in North and Latin America

Dependent Variable:	**Sign and Significance of the Coefficients**			
Tax Morale	**TRUST**			**PRIDE**
Countries	TRUST IN GOVERN.	TRUST IN PRESIDENT	TRUST PUBL. OFFICIALS	
COUNTRIES POOLED				
Latin America (WVS 1995-1997)			+	+
Latin America (Latinobarómetro 1998)		+		
SPECIFIC COUNTRIES				
USA				
1987 (Taxpayer Opinion Survey)			+	
Canada				
1990 (WVS)	+			+
Costa Rica				
1998 (Latinobarómetro)		+		

Notes: Dependent variable: tax morale. +: significant positive coefficient, (+), (-), positive, respectively negative coefficient sign without being significant, (±) positive and negative sign of the coefficient without being significant.

Table 12: The Effects of Trust and National Pride on Tax Morale in Transition and Asian Countries

Dependent Variable:	**Sign and Significance of the Coefficients**			
Tax Morale		**TRUST**		**PRIDE**
Countries	**TRUST IN GOVERN.**	**TRUST LEGAL SYS.**	**TRUST PUBL. OFFICIALS**	
COUNTRIES POOLED				
Transition Countries (WVS 1989-1993)		+		+
Transition Countries (WVS 1995-1998)	+	+	+	+
Asia (WVS 1995-1997)	+	+		
SPECIFIC COUNTRIES				
TRANSITION COUNTRIES				
Former Soviet Union Countries				
Russia 1991 and 1995 (pooled)	+	+		+
Estonia 1990 and 1996 (pooled)	+	+		+
Latvia 1990 and 1996 (pooled)	+	+		+
Lithuania 1990 and 1996 (pooled)	+	+		+
Belarus1990 and 1996 (pooled)	+	+		+
Central/Eastern Europe				
Poland 1989 and 1997 (pooled)	+	+		+
Bulgaria 1990 and 1997 (pooled)	+	+		+
Slovenia 1992 and 1995 (pooled)		+		+
ASIA				
India				
1995/1996	+			+
1990 and 1995/1996 (pooled)	+	+		+
Japan				
1995		+	+	(+)
1981, 1990 and 1995 (pooled)		+		+

Notes: Dependent variable: tax morale. +: significant positive coefficient, (+), (-), positive, respectively negative coefficient sign without being significant, (±) positive and negative sign of the coefficient without being significant.

Table 13: The Effects of Trust and Pride on Tax Morale in Transition and Asian Countries

Dependent Variables:	**Sign and Significance of the Coefficients**			
Tax Compliance and Tax Morale	**Democracy**			**Federalism**
Countries	DIRECT DEMOCRACY	VOTING	PRO DEMOCR. ATTIT.	LOCAL AUTONOMY
SPECIFIC COUNTRIES				
Switzerland				
1996 (WVS)	+			+
1999 (ISSP)	+			+
Experiment		+		
Switzerland and Costa Rica (pooled)				
Experiment		+		
Experiment		+		
USA				
1995 (WVS)	+			
1987 (Taxpayer Opinion Survey)	+			
Spain				
1990 (WVS)			+	
Japan				
1995 (WVS)			+	
India				
1995/1996 (WVS)			+	
COUNTRIES POOLED				
Latin America (WVS 1995-1997)			+	
Transition Countries (WVS 1995-1998)			+	

Notes: Dependent variable: tax morale. +: significant positive coefficient.

2.3 Institutions

Constitutional requirements that define the basis of the politico-economic process are also supposed to influence tax morale. Direct democracy and local autonomy, which set the rules between taxpayers and the state at the constitutional level, are key factors. The results indicate that both, a more direct democracy and a stronger local autonomy lead to significantly higher tax morale in Switzerland and in the United States.

Direct political participation possibilities by taxpayers using popular referenda and voter initiative can strengthen the acceptance of government decisions and hence the willingness to contribute to the costs of public goods and services. Direct democracy gives government decisions a particularly high authorization and thus makes taxpayers feel responsible for the decisions. This holds to a certain extent even with respect to minorities, which could not succeed at the ballots. If the process of decision-making is perceived as being fair and trans-

parent, taxpayers are ready to contribute to public goods and services even in cases, where other citizens, but not themselves, are benefiting from such decisions. Citizens derive procedural utility from political participation rights (Benz 2005).

The extent to which taxpayers can participate in the political decision making process has even a positive impact on their perceived satisfaction with life (Frey and Stutzer 2002). Compared to purely representative systems, direct democracy leads to a different type of communication among citizens and also between citizens and representatives. The possibility of deciding for themselves on basic political issues provides incentives for citizens to collect more information. This information is not only needed to make "correct" decisions at the ballots, but also in order to participate in the dialogue with other citizens. Thus, to be well informed about political issues is not only a voluntary contribution to a public good, but has also at least some characteristics of a private good, in order to signal competence to others (see Torgler and Schaltegger 2005 in the case of directly voting on a tax amnesty). Moreover, as citizens are generally better informed in direct than in purely representative democracies, politicians have less leeway to pursue their personal interests instead of those of the general public. Finally, citizens feel more responsible for their community.

In the course of the public debate, at least in parts of the citizenry, a learning process occurs. Since many citizens are confronted with arguments of both sides, those opposing and those favoring a certain policy outcome, they are induced to consider each proposal anew. This can lead to a revision of their personal opinion. Therefore, the possibility also emerges that citizens examine the extent to which their preferences generalize.

In order to evaluate the impact of direct democracy on tax compliance Pommerehne and Weck-Hannemann (1996) have conducted an empirical analysis among the Swiss cantons. With a number of possible economic and institutional factors they try to explain the amount of non-declared income in the Swiss cantons. One of the institutional factors is the extent to which people can directly decide on budgetary issue via referenda and initiatives. Since among the Swiss cantons a huge variety of elements of direct democracy are in use, the cantons represent a natural laboratory to investigate the question. The results show that among other important determinants the extent of direct legislation has a positive and significant impact on tax compliance. In fact, the difference is important: cantons that make strong use of direct democracy face a rate of tax evasion that is about 30 percent lower than it is in cantons that rely more on the model of representative democracy. In order to evaluate the importance of this effect, it is interesting to notice that one must triplicate the detection probability to achieve the same

effect. Of course, the latter would also imply a lot of costly government efforts. Insofar, to strengthen direct legislation seems to be an effective way to fight tax evasion at low costs. Furthermore, the study shows that higher marginal tax rates lead to higher tax evasion.

Table 13 also shows that a higher pro democratic attitude leads to higher tax morale in Latin America and in transition countries as well. A move toward more democracy as we observe in transition countries (see, e.g., Frey 2002) might help to enhance tax morale and civic virtue over time.

Moreover, decentralization of taxing power is important in addition to direct legislation. Voters trust more in local government decisions than in central government decisions. Possible reasons for that are: Firstly, voters have more control over local decision-makers who they often know personally. Secondly, at the local level, decision-makers have more knowledge about taxpayers' preferences, which gives them the possibility to better tailor governmental services according to the specific needs of their constituencies. Unfortunately, up to now there is hardly any empirical evidence on the impact of decentralization on tax compliance (for an exception see Torgler 2003g and Torgler and Werner 2005). This eventually represents a fruitful avenue for further research.

2.4 Deterrence and Perceptions, the Tax System and the Tax Administration

Table 14 shows that tax policy should maintain a high level of social capital. If people believe that others are honest their willingness to pay taxes increases. Reciprocity is a key factor: if individuals notice that many others evade taxes, their intrinsic motivation to comply with taxes decreases. Evasion is a signal that intrinsic motivation is not recognized. Thus, taxpayers get the feeling that they can as well be opportunistic and the moral costs of evading taxes decrease. On the other hand and similar to the argumentation in Section 2.2 on the determinant "trust", *Table 14* indicates that if the tax administration tries to be honest, fair, informative, and helpful, acting as a *service* institution and thus treating taxpayers as partners and not "inferiors in a hierarchical relationship, taxpayers have stronger incentives to pay taxes honestly" (Frey 2003, p. 11).

Table 14: Deterrence and Perceptions, the Tax System and the Tax Administration

Variables	Countries						
	Switzerland (CH)		US	Latin America		CH and CR (pooled)	
	WVS (1996)	ISSP (1999)	TOS 1987	Latin America LB 98 (pooled)	Costa Rica (CR) LB 98	Exp. C. XVII	Exp. C. XXII
Dependent Variable: Tax Morale							
Independent Variables							
a) Deterrence Factors						-	-
FINE RATE	(-)	(-)				-	-
AUDIT PROBABILITY	(+)	(±)					
HAVING BEEN AUDITED			-				
b) Tax System							
INDIVID. INCOME TAX RATE	(-)	(-)					
FAIRNESS OF THE TAX SYSTEM			+				
COMPLEXITY OF THE TAX SYS.			(-)				
c) Tax Administration (TA)							
POSITIVE ATTIT. TOWARDS TA			+				
d) Taxpayers' Perception							
TAX EVASION/AVOIDANCE			-				
PROBABILITY OF AUDIT			-	(-)			
FEAR OF GETTING CAUGHT			+				
TRUST PEOPLE OBEY THE LAW			+	+	+		

Notes: Dependent variable: tax morale. +: significant positive coefficient, (+), (-), positive, respectively negative coefficient sign without being significant, (±) positive and negative sign of the coefficient without being significant.

Connected to these findings on the determinants of tax morale we observe that there has been a noticeable shift toward a more balanced set of strategies in tax administrations. In many countries there is an increased emphasis on quality, customer service and reasonable and fair treatment of taxpayers. However, studies that investigate the impact of such a shift are still hardly available (for exceptions, see Torgler 2004b for Japan and Torgler and Murphy 2004 for Australia).

Japan, for example, offers a good example for a consequent strategy with the aim to intensify an interaction between tax administration and taxpayers based on trust. After the reorganization in 1949, the Japan tax administration had a high rate of tax delinquency (around 40 percent). A too fast implementation of the self-assessment system and high tax burdens frustrated Japanese taxpayers. The following reforms aimed at reducing the tax burden, simplifying the tax returns and improving taxpayers' assistance helped to increase tax compliance. Today, Japan is known for a high degree of tax morale, which might be influenced by the intensive interaction between the tax administration and the taxpayers based on trust.

Another example is Australia. The 1980s saw public administration being faced with growing state and public demands to become more market-focused, service oriented, open

and efficient. In response to that, the Australian Taxation Office (ATO) adopted a new, efficiency-oriented and customer-focused organizational structure. Most interestingly, instead of focusing on compliance management, risk control, or structuring the application of enforcement discretion, the ATO focused more on service, customer needs, quality, transparency and process improvement. In fact, the ATO was amongst the first tax administrations in the world to implement a new client-based organizational structure (the client based model is where staff is assigned to units that focus on specific groups of customers; for example, salary and wage earners, small business income taxpayers, and large business income tax payers)[3]. One of the advantages of such a client-based structure is that it allows tax administrations to better match their enforcement and educational programs to the compliance patterns of different groups. This helps delivering higher quality service to taxpayers (see Verhorn and Brondolo 1999). If taxpayers recognize that such an approach is likely to achieve better compliance, it may also influence their own tax morale. Thus, a client-focused approach is likely to increase trust among taxpayers, as taxpayers' needs are being considered more thoroughly in the regulatory process.

IV. DIRECTIONS FOR FUTURE RESEARCH

In the last section we provided an overview on some of the determinants of tax morale that have been isolated so far. However, there is a lot of unexplained and empirical evidence is essential due to the lack of insights. In their overview, Andreoni, Erard and Feinstein (1998) state: "Although many empirical studies of noncompliance have been conducted during the past decade, we believe that the empirical literature is still in its youth, with many of the most important behavioral hypotheses and policy questions yet to be adequately investigated" (pp. 835-836). In the following, we concentrate on some further topics we believe are important for future research.

1. Complexity of the Tax System

Can simplicity of the tax system induce a higher tax compliance rate? Is complexity correlated with tax evasion? In general, simplicity is a major issue in tax reform concerns. A good tax system should be simple and easy to understand. Complexity may result in unintentional non-compliance if taxpayers have problems in filling out the tax form. It can reduce the moral costs of evading taxes and might impose costs to the taxpayers. A simpler tax law would re-

[3] Prior to this, a function-based structure was used by the ATO (e.g., a separate division for processing tax returns, another for auditing taxpayers, and another for collecting arrears).

duce taxpayers' expenditure in time and money to comply with the tax law. Until now, only little empirical evidence is available regarding the effects of a simplification of the tax system on tax compliance and tax morale. This topic can be elucidated by surveys and (field) experiments. Experiments and field experiments can help to get insights into the direct causality of this complex area. Surveys on the other hand can give a better picture of whether a higher perceived complexity leads to a lower or a stronger tax morale or tax compliance.

2. Business Tax Evasion

In most of the studies on tax compliance, research has focused on personal income tax compliance. Business tax evasions in general and VAT compliance in particular have received very little attention. This surprises taking into account the economic importance of the business sector and importance of business taxation for the tax administration. Work in this area is therefore highly relevant. Certainly, VAT has the advantage that it is more difficult to evade than a general retail sale taxes. However, there are possibilities to evade VAT taxes and Agha and Haughton (1996) provide a detailed list including understatement of sales, inflation of claims for VAT paid inputs, claiming credit for tax paid on inputs used in producing goods which are exempt from VAT, non-registration for VAT, diversion of zero-rated exports to the domestic market or claiming that the transaction is not a taxable event. Agha and Haughton (1996) report from audits in France in 1984 that for two-thirds of those audited had understated the value of taxable sales, a quarter of them fraudulently. Two-fifths of those audited had overstated the value of taxable inputs. They also provide a summary for VAT tax evasion in different countries. For example, in the late 70s, 40% of the VAT revenues went uncollected in Italy and in the Netherlands, a third of all firms had evaded some VAT.

In general, Agha and Haughton's results indicate that VAT compliance improves with a lower VAT rate, fewer rates, a smaller population, more learning time and greater spending in the tax administration. They also conclude that a single rate on a broad base is the ideal form of VAT. It not only increases the degree of compliance but also lowers the costs of administration. Interestingly, there is evidence for a political trade-off between raising a smaller amount of revenue with an efficient broad-based, single and low rated VAT and raising a higher amount of revenue with higher VAT rates but on a narrow base with multiple rates. However, the authors state that this result must be treated with caution, "because recommendations based on cross-country comparisons are apt to have a "one size fits all" quality, which overlooks the history, traditions and special features of any given country and which are so important to the policy analyst. Nor are distributional effects treated here" (p. 307).

All in all, knowledge on tax morale in the case of business taxes is very limited so far. For example, it would be important to have evidence on tax compliance for different business areas covering topics such as deterrence, equity, competition, morality, attitudes towards VAT, the tax system, the administration, the tax burden (e.g., corporate taxes), other businesses, other businesses' compliance efforts, perceived seriousness to commit VAT etc.. This could be conducted using different methods.

V. CONCLUSIONS

The economic literature has made major attempts to integrate efficiency and equity considerations into the theory of optimal taxation. Though this literature has yielded important insights on optimal tax policy issue, it is not free of criticism. Especially, the narrowness of the optimal taxation approach is subject to various critics. For example, Brennan and Buchanan (1980) criticize the optimal taxation literature due to its institutional vacuum. The same can be applied to tax compliance and tax morale. Tax compliance has been subject to a variety of academic disciplines and also the revenue services. One branch of research analyzes tax compliance in terms of a pure cost-benefit calculus of an individual taxpayer. According to this view, the level of enforcement measures like controls and fines as well as the risk aversion of a taxpayer determine the level of tax compliance. The other branch of research is broader and incorporates many other determinants of taxpayer behavior into account, like socio-economic factors, the politico-institutional background or the tax agency behavior and stresses the relevance of tax morale or social norms to understand the level of tax compliance.

For conducting fiscal policy, results and conclusions obtained in tax morale research are of considerable importance. First, it can provide insight in a more efficient way of raising revenues since the interaction between the taxpayer and the tax authority is taken into account. Second, this research points to a broader understanding of tax compliance where aspects of deterrence (audits and penalties), government regulation, opportunity costs (migration costs and employment status), the quality of publicly provided goods, the tax system (complexity, progressivity and incidence), treatment of taxpayers by the tax authority (transparency, partnership and generosity) and the homogeneity or heterogeneity of the society should be systematically evaluated.

In this paper, we have provided a survey of the research that has been conducted on the magnitude and the determinants of tax morale. In particular, we have concentrated on fiscal policy implications. Additionally, we discussed directions for future research on two im-

portant areas, which may be useful to tackle in the future: the impact of the complexity of the tax structure on tax morale and business tax evasion.

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