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## A Tax Morale Approach to Compliance: Recommendations for the IRS

Marjorie E. Kornhauser

*Sandra Day O'Connor College of Law, Arizona State University*

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by

*Marjorie E. Kornhauser*

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**A TAX MORALE APPROACH TO COMPLIANCE:  
RECOMMENDATIONS FOR THE IRS**

*by*

*Marjorie E. Kornhauser\**

**SUMMARY**

Why do people follow the law? The answer, under the traditional theory of compliance, is fear of detection and punishment. The deterrence model, however, accounts for only a minor portion of actual compliance levels. It has such poor explanatory power because it assumes that the decision to comply is based solely on a rational cost-benefit analysis in which people weigh the benefits of non-compliance against the costs of detection and penalties. Recent literature reveals, however, that the decision to comply is not purely rational. Rather, personal values, social norms, and non-rational cognitive processes also strongly affect the decision.

What holds true for law in general holds true for tax compliance specifically. Traditional methods of enforcement through audit and penalties explain only a small fraction of voluntary tax compliance. Theorists and researchers attribute the vast majority of compliance to what they loosely describe as internal motivations or “tax morale.” The field is still young, the subject complex, and some of the empirical data is inconclusive. Nevertheless, the literature clearly indicates that tax morale plays a major role in tax compliance.

Although neither the exact components of tax morale nor the precise mechanisms by which they work have yet been fully delineated the literature has identified certain elements. Research shows that tax compliance is affected by (social and personal) norms such as those regarding procedural justice, trust, belief in the legitimacy of the government, reciprocity, altruism, and

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\*©Marjorie E. Kornhauser, Professor of Law, Sandra Day O'Connor College of Law, Arizona State University. This article appeared in the December 31, 2007 Annual Report to Congress of the National Taxpayer Advocate, which commissioned this research.

identification with the group. Cognitive processes, such as prospect theory, also influence an individual's reaction to tax issues. Studies also indicate that certain demographic factors such as age, gender and education correlate with the tax morale.

The components of tax morale, like internal motivators in other areas of the law, are not static. They interact with each other and the environment and are influenced by each individual's own cognitive framework. Consequently, an external agent, such as the IRS, can influence tax morale norms and thereby tax compliance. It can activate compliance norms in a variety of ways including education, properly framing communications, fair procedures, and a regulatory framework that incorporates current and future findings of tax morale research into its operations and dealings with taxpayers.

The Report makes three major recommendations. First, the IRS should establish a department devoted solely to exploring tax morale issues and implementing the findings. Second, the IRS should adopt a tax morale approach to tax compliance that recognizes the importance of taxpayers' internal motivations and the effects on these motivations of societal conditions and institutions (such as the IRS) that interact with them. Third, using behavioral science research, the IRS should implement ongoing educational (long term and short term) programs and media campaigns. Since the subject of this Report is tax compliance of individual taxpayers, both the literature review and the recommendations focus on individuals. Both the tax morale concept and this Report, however, are relevant for all taxpayers.

## I. INTRODUCTION

If people hate taxes so much why do they pay them? The common, seemingly obvious, answer – fear of being caught cheating – is only a partial answer. In fact, the “obvious” answer – based on the rational cost/benefit analysis of traditional economic theory – explains so little of tax compliance that “[t]he puzzle of tax compliance is why people pay taxes instead of evading them.”<sup>1</sup> The key to the puzzle is “tax morale,” the collective name for all the non-rational factors and motivations – such as social norms, personal values and various cognitive processes – that strongly affect an individual's voluntary

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1. Lars P. Feld & Jean R. Tyran, *Tax Evasion and Voting: An Experimental Analysis*, 55 *Kylkos* 197, 197 (2002). The traditional model of deterrence, based on detection and penalties, states that compliance with the law is a function of enforcement levels; a rational individual weighs the costs of non-compliance against the benefits. In the tax evasion context, this model states that a risk-averse taxpayer will engage in an amount of tax evasion that will maximize expected utility of income which is a function of “(i) the probability of detection, (ii) the penalty tax rate applied when tax evasion has been detected, (iii) the marginal tax rate, and (iv) the level of true income.” Werner W. Pommerehne & Hannelore Weck-Hannemann, *Tax Rates, Tax Administration and Income Tax Evasion in Switzerland*, 88 *Pub. Choice* 161, 162 (1996).

compliance with laws.<sup>2</sup> Higher tax morale correlates with higher tax compliance.

Although the exact components of tax morale are not yet fully delineated, Congress and the IRS should begin now to shape and administer income tax laws in accordance with tax morale findings. Delay can only increase the chance that voluntary compliance will deteriorate given the interaction of an individual's tax morale with elements of the external environment, such as other people and institutions. The tax gap, for example, is more than a problem of lost revenue; it is a visible sign of non-compliance that can create a downward spiral. Non-compliance among other taxpayers can decrease an individual's own tax morale and compliance.<sup>3</sup> Once tax morale dips, it is hard to restore it to prior levels.<sup>4</sup> Ironically, then, the more the tax gap is publicized, the greater this danger becomes. Congress and the IRS must act now to narrow the tax gap and to foster compliance generally.

This Report offers the IRS several concrete suggestions for improving individual taxpayer compliance based on the tax morale literature. Part II discusses methodology and the limitations of empirical research. Part III briefly

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2. "Voluntary" in this context, of course, means compliance without any actions taken by the tax collection agency. The literature is vast. Tax morale research is part of the more general field of inquiry into why people comply with laws generally. Two seminal books in the larger field are: Robert C. Ellickson, *Order without Law: How Neighbors Settle Disputes* (1991); Tom Tyler, *Why People Obey the Law* (1990).

In the tax evasion context, the traditional deterrence model states that a risk-averse taxpayer will engage in an amount of tax evasion that will maximize expected utility of income which is a function of "(i) the probability of detection, (ii) the penalty tax rate applied when tax evasion has been detected, (iii) the marginal tax rate, and (iv) the level of true income." Michael Allingham & Agnar Sandmo, *Income Tax Evasion: A Theoretical Analysis*, 1 *J. Pub. Ec.* 323 (1972); Kim M. Bloomquist, *Tax Evasion, Income Inequality and Opportunity Costs of Compliance*, *Nat'l Tax Ass'n Proc.*, *Ninety-Sixth Ann. Conf.* 2003, 19 (2004).

The literature on tax morale alone is large. Some literature reviews include: James Andreoni, Brian Erard & Jonathan Feinstein, *Tax Compliance* 36 *J. Econ. Lit.* 818, 835 (1998)(only a few empirical studies on tax compliance before 1980); Benno Torgler, *Speaking to Theorists and Searching for Facts: Tax Morale and Tax Compliance in Experiments* 16 *J. Econ. Surv.* 657 (2002). That the majority of knowledge in this area has occurred only in the past 5-7 years is evidenced by the rudimentary knowledge provided in the 1998 Andreoni et al. review of the literature, as compared to later research.

3. Bruno S. Frey & Benno Torgler, *Tax Morale and Conditional Cooperation*, 35 *J. Comp. Econ.* 136, 153 (2007).

4. See, e.g., Jon S. Davis, Gary Hecht & Jon D Perkins, *Social behaviors, enforcement, and tax compliance dynamics*, 78 *Acc. Rev.* 39, 39 (2003); Ernst Fehr & Armin Falk, *Psychological foundations of incentives*. 46 *European Econ. Rev.* 687 (2002); Jan Schnellenbach, *Tax Morale and the Taming of Leviathan*, 17 *Const. Pol. Econ.* 117, 130 (2006); Michael Wenzel, *Misperceptions of Social Norms about Tax Compliance: From Theory to Intervention*, 26 *J. Econ. Psychol.* 862 (2005).

describes the tax morale literature, focusing on the main findings regarding: 1) cognitive and affective processes; 2) personal and social values/norms, especially procedural justice, legitimacy, reciprocity, and trust; 3) external activation and suppression of tax morale; 4) demographic factors, and 5) a new tax morale model for tax administration.

Part IV contains recommendations for the IRS. It presents three major recommendations and several more specific proposals for the IRS to improve individual taxpayers' voluntary compliance. First, the IRS should establish a department devoted solely to exploring tax morale issues and implementing the findings. Second, the IRS should adopt a tax morale model of operation that incorporates the findings of the research and seeks to respond to, and strengthen taxpayers' internal motivations to comply. Third, using tax morale research, the IRS should implement ongoing educational (long term and short term) programs and media campaigns. Although sticks as well as carrots are needed to ensure compliance, this Report examines only the carrots. Part V provides a short conclusion.

## II. METHODOLOGY AND ITS LIMITATIONS

### A. Methodology

This Report surveys recent literature concerning the "tax morale" model of tax compliance. It examines some of the cognitive processes involved, such as framing, but it concentrates on the moral, psychological, and social factors influencing tax compliance.

The Report reviews a large quantity of tax morale literature but it is not comprehensive. It focuses on literature published in the last 5 years, which builds on and refines the first wave of literature. Within this time period, the Report reviews a substantial amount of the existing literature but not all since a comprehensive review would be both extremely lengthy and repetitive.

The Report examines empirical tax compliance literature in a variety of related fields such as behavioral economics and psychology, cognitive psychology, social psychology, and law, paying particular attention to tax morale (sometimes called taxpayer ethics.)<sup>5</sup> Some of the studies pertain to other countries, or are comparative in nature. In order to provide greater context, the Reviewer also briefly examined literature pertaining to norms, cognition, and the law generally.

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5. Benno Torgler & Friedrich G. Schneider, What Shapes Attitudes Toward Paying Taxes? Evidence from Multicultural European Countries (May 2006). IZA Discussion Paper No. 2117 at <http://ssrn.com/abstract=901247>, at 3 (citing earlier studies).

For added perspective, the reviewed literature includes materials in the fields of compliance with environmental laws and advertising/marketing. Compliance with environmental law has many similarities to tax compliance. Although some environmental laws do contain traditional “stick” deterrents such as fines, enforcement at the individual level largely depends on voluntary compliance, as in tax. Moreover, environmental and tax compliance share common collective action problems since the individual’s benefits from compliance are often attenuated and individual behavior is largely not visible to others. Marketing/advertising literature – with its long history of researching and applying knowledge of the psychological and social aspects of human behavior – is also relevant to tax compliance. Moreover, unlike the artificial environment of a controlled lab experiment, marketing occurs in the real world. Consequently, results in this field allow for the interplay of a variety of influences and may be observed over time.

The literature was obtained through searches on various databases such as: Lexis, Westlaw, Science Direct, EconLit, and JSTOR as well as various web pages such as that of the IRS and ATO.

In addition to the literature review, the writer interviewed several professionals in the UK – both in Treasury and HMRC – in order to obtain an overview of the UK perspective on compliance. These interviews occurred in May 2007.

### *B. Limitations of the Literature*

Both theoretical and empirical research have limitations. Theories, of course, are limited by their point of view and their assumptions. Empirical research also has limitations. For example, how questions are phrased, and in what order, can affect responses. The gap between belief, intention and action can also result in unreliable responses. Self-reporting creates problems – there is a difference between what people report they believe and/or would do and what they actually believe or would do. This results from a variety of factors ranging from the fact that people often imperfectly perceive their own motivations, to the fact that people often report what they think the interviewer wants or what they think (or are told) the topic is.<sup>6</sup>

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6. Self-perception theory, in fact, is based on the assumption that people have imperfect knowledge of their motivations. See, e.g. Fehr & Falk, *supra* note 4, at 714 (“A crucial assumption of self-perception theory is that individuals do not have perfect knowledge about the reasons for performing a task.”). Accord, Eric Kirchler, Apolonia Niemirowski & Alexander Wearing, Shared subjective views, intent to cooperate and tax compliance. Similarities between Australian Taxpayers and Tax Officers, 27 *J. Econ. Psychol.* 502, 514 (2006)(imperfect self-perceived motivation); Torgler & Schneider, *supra* note 5, at 11 (people overstate their compliance); Viswanath Umashanker Trivedi, Mohamed Shehata & Stuart Mestelman, Attitudes, Incentives, and Tax Compliance, 53 *Canadian Tax J.* 29, 60 (2005)(lab experiments do not reflect real-



Sampling issues also influence empirical results. The population studied may not be representative. Different groups have different characteristics (e.g., age, gender) which may obscure the causes of the results. Did the subjects, for example, respond in the way they did simply because of the apparent variable (e.g. presentation of numbers of taxpayers who evade) or were their reactions also influenced by the fact that the majority of the sample population was a particular age or gender. Results can also be skewed by what is called the “isolation” effect which causes people to focus on the information presented to them and ignore that which is not.<sup>7</sup> As a consequence people’s decisions frequently do not form a consistent whole. In the experimental context this means that a different outcome might occur if the survey question, or experiment, were presented in a different context with different salient facts.

One of the more important limitations of empirical research regarding compliance is the fact that much of the research has been conducted in a controlled laboratory situation. Although this allows researchers to isolate individual effects, it also weakens the results. In any controlled experiment, there is always the question of whether what the subject does in the controlled environment represents what s/he would do in the real world. This is amplified in the tax compliance area because it is often the confluence of a variety of factors that influence compliance.<sup>8</sup> Moreover, many aspects of tax compliance develop over time so that even a laboratory study that involves a sequence of “games” or interactions may not capture the effects that develop over time. It is important to keep these limitations in mind when reading this literature review.

### III. LITERATURE REVIEW

Tax morale refers to taxpayer attitudes and beliefs – not behaviors – but researchers are investigating the connection between the former and the latter. At its broadest, tax morale is an imprecise term – encompassing all the non-enforcement aspects of tax compliance. Current research is deconstructing this undifferentiated black box<sup>9</sup> into its components. Some of these components are

life decisions, self-presentation problems ranging from poor memory of past behavior to desire to look good in eyes of experimenters).

7. Edward McCaffery & Jonathan Baron, *The Political Psychology of Redistribution*, 52 *UCLA L. Rev.* 1745, 1752, 1791 (2005).

8. See, e.g., Robert B. Cialdini, *Social Motivations to Comply: Norms, Values, and Principles in 2 Taxpayer Compliance* 200, 201 (Jeffrey A. Roth & John T. Scholz eds., 1989).

9. Richard M. Bird, Jorge Martinez-Vasquez & Benno Torgler, *Tax Performance in Developing Countries: The Role of Demand Factors*, *Nat’l Tax Ass’n, Proc. Ninety-seventh Ann. Conf.* 2004, 284, 287 (2005). (tax morale is the “intrinsic motivation to pay taxes”); Lars P. Feld, & Bruno S. Frey, *Trust Breeds Trust: How Taxpayers Are Treated*, 3 *Econ. of Governance* 87, 88-9 (2002); Torgler & Schneider, *supra* note 5, at 3. (tax morale as the “moral obligation to pay taxes, a belief in

intrinsic factors – individual traits that motivate a person to comply such as a personal sense of integrity or degree of altruism. Others more directly relate to external conditions or societal norms such as procedural justice, trust in government, or the form of government.<sup>10</sup> External and internal factors, however, interact and researchers are examining the ways in which internal motivations interact with external ones, each influencing and affecting the other and how cognitive processes can influence both.

This Part provides a short overview of three major areas in the rapidly growing field of tax morale research: cognitive and affective processes, social norms, personal values/norms, and demographic factors. It then briefly describes a new model of a tax authority, frequently called a responsive or self-regulatory model, based on tax morale findings.

#### *A. Cognitive and Affective Processes*

Cognitive and affective processes are unconscious mechanisms that influence a person's perception and response to information, people, and the environment. Two cognitive processes are of particular importance to compliance. One is "framing." The manner in which acts, stimuli, or situations are presented – or framed – can affect a person's reaction to it. This effect is evident in surveys that result in different responses depending on what order questions are posed, for example, or whether the question is posed in the positive or negative. Labels also matter. For example, people generally react more favorably when a payment is called a fee rather than a tax.<sup>11</sup> Framing also affects various other tax attitudes such as preferences for progressive or flat rates, levels of taxes, and government spending.<sup>12</sup> One of the most important types of framing involves prospect theory, described below.

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contributing to society by paying taxes.") Schnellenbach defines tax morale 'pragmatically' 'as the phenomenon that taxpayers (1) on average evade less taxes than an optimization calculus incorporating only expected judicial punishment and reasonable levels of risk aversion would predict and (ii) systematically adjust their evasion levels according to how satisfied they are with public policy, processes of collective decision-making and the quality of their relationship to authorities.'" Schnellenbach, *supra* note 4, at 118.

10. See, e.g., James Alm & Benno Torgler, Culture difference and tax morale in the United States and in Europe, 27 *J. Econ. Psychol.* 224, 226 (2006) (arguing that "tax morale is likely to be influenced by such factors as perceptions of fairness, trust in the institutions of government, the nature of the fiscal exchange between taxpayers and government, and a range of individual characteristics.")

11. McCaffery & Baron, *supra* note 7, at 1760. This is not true, however, in regards to existing services that are funded by a general tax. In that situation, respondents do not prefer a fee because they perceive it as paying for a service/good that they are already getting for "free." *Id.*

12. *Id.*

The other important cognitive process is what this Report labels “shortcuts.” Shortcuts encompass a variety of overlapping, somewhat amorphous, concepts variously called heuristics,<sup>13</sup> cultural cognitions<sup>14</sup> or schemas. Collectively, they are the mechanisms that allow people to respond quickly to the otherwise overwhelming amount of stimuli that bombard them daily. Shortcuts create general “rules of thumb” that allow individuals to efficiently acquire, store, organize and retrieve knowledge; they influence a person’s perception of new data and his/her reactions to it. Shortcuts involve both cognitive and affective processes and are the product of various factors such as cognitive processes (such as framing), psychological traits, prior experiences, social and personal norms.

Different world views or cultural cognition shortcuts incorporate different norms and values. A person with an individualist world view, for example, strongly incorporates the norms of self-reliance, independence, and effort whereas the values of a person holding the opposite collectivist view would emphasize equality, reciprocity, cooperation, and so forth. Some world views (cultural cognitions or schemas) are associated with particular demographic groups – racial, religious, regional, gender, or age-based for example.

Shortcuts generally do not change in the face of new information because they are based on values not information.<sup>15</sup> As a consequence, Kahan and Braman argue that successful policies must be framed so as to appeal to people with different views. Tradable emission permits are an example of such a policy.<sup>16</sup> Individualists like the permit policy, they claim, because its market mechanism appeals to their belief in private enterprise; “hierarchists” support it because it leaves power in the hands of powerful commercial entities, and egalitarians and collectivists support it because it recognizes their goal of improving air pollution and the need to constrain industry.<sup>17</sup>

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13. See, e.g. John T. Scholz & Neil Pinney. *Duty, Fear, and Tax Compliance: The Heuristic Basis of Citizenship Behavior*, 39 *Am. J. Pol. Sci.* 490, 491 (1995). (heuristic as cognitive short cut).

14. Dan Kahan & Donald Braman, *Cultural Cognition and Public Policy*, 24 *Yale L. & Policy*, 149 (2005).

15. *Id.*, at 152-3.

16. *Id.* at 169.

17. *Id.* French abortion reform that ‘conditioned abortion on an unreviewable certification of personal “distress” is another example. That policy made it possible for both religious traditionalists, who interpreted certification as symbolizing the sanctity of life, and egalitarians and individualists, who interpreted unreviewability as affirming the autonomy of women, to see their commitments affirmed by the law.’ *Id.* at 168.

*1. Framing: Prospect Theory*

Prospect theory is probably the framing effect most relevant to tax compliance.<sup>18</sup> The theory, which explains how people evaluate risk, holds that people are risk averse in regards to gains but risk-seeking in regards to loss. Consequently, the manner in which a decision is framed will affect a person's willingness to take risks. In income tax, for example, whether an issue is framed as a bonus for those with children (such as a child credit) or a penalty for the childless will affect a taxpayer's attitude toward the provision.<sup>19</sup> It also means that a taxpayer will be more willing to take risks (not comply) when the issue is framed as a loss (penalty from an audit) than as a gain (a bonus from a refund).<sup>20</sup> Consequently, the manner in which information is communicated to a taxpayer can have a major impact on his willingness to comply with the tax laws.

According to prospect theory, tax compliance should increase if paying taxes is seen as a gain not a loss. If a taxpayer views his situation as interconnected with the nation's either because s/he is a collectivist (see world view below) and/or through identification with the nation, then taxpaying is more likely to be viewed as a gain than a loss.<sup>21</sup> One study suggests that if a taxpayer views taxes as a national obligation, then after tax income is the taxpayer's reference point and therefore

tax compliance decisions are made in the gain domain, which leads taxpayers to pursue risk averse behavior. On the other hand, if the taxpayer considers paying taxes as loss, then his/her reference point would be their income before tax. In this case, the taxpayer will be likely to engage in risk-seeking behavior."<sup>22</sup>

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18. John Cullis, Philip Jones & Alan Lewis, Tax Framing, Instrumentality and individual differences: Are there two different cultures? 27 *J. Econ. Psychol.* 304, 306 (2006). See, generally, *Choices, Values, and Frames* (Daniel Kahneman & Amos Tversky eds., 2000).

19. McCaffery & Baron, *supra* note 7, at 1758.

20. Cullis et al., *supra* note 18, at 306.

21. See, Phillip Hansen, *Taxing Illusions, Taxation, Democracy and Embedded Political Theory* 16 (2003)(for citizens "the issue of what politics means and what kind of democracy is desirable turns on a fundamental question...: To what extent can my purposes be fulfilled only together with others; indeed to what extent are my purposes *our* purposes. . . . With respect to taxation, this raises the question of whether taxes are charges imposed on us by remote political authorities we are always reluctant to pay and do so only because we are coerced, or whether they are self-imposed levies, expressions of our commitment to the well-being of all.").

22. Viswanath Umashanker Trivedi, Mohamed Shehata & Bernadette Lynn, *Impact of Personal and Situational Factors on Taxpayer Compliance: An Experimental Analysis* 47 *J. Bus. Ethics* 175, 179 (2003).

## 2. Short Cuts/Worlds Views

Several world views with deep roots in America are especially relevant to tax compliance. Two interrelated ones involve the twin political foundations of American democracy: equality and liberty. The first world view concerns the relationship of the individual to the group (individualistic versus collective orientation; the second view concerns the nature of society (hierarchical versus egalitarian).<sup>23</sup> Individualistic, hierarchical people emphasize negative liberty more than equality and therefore look to the individual, not the government, to solve social problems. Such a taxpayer will be less likely than a collectivist/egalitarian taxpayer – who emphasizes equality and positive liberty – to support higher or redistributive taxes.

A collectivist-oriented and/or egalitarian individual will be more willing to pay taxes even if her tax burdens exceed her individual benefits (i.e., no material fiscal exchange equity) if the taxes help the group. Moreover, this person might consider the reduction of inequality and the provision of goods to others a benefit when determining whether there is fiscal equity.<sup>24</sup> She will see paying taxes as a gain, fulfilling personal desires and civic obligations and not just a loss of personal income. As a result, according to prospect theory, she will be risk-averse and more willing to comply.

Two other “schemas” or “world views” with deep historical roots in American history and politics can negatively influence tax compliance – a general anti-tax schema and an anti-establishment schema. As to the first, although tax compliance – and tax morale – is relatively high in the United States compared to other countries, many Americans harbor strong anti-tax sentiments which are part of a national anti-tax schema that reaches back to the founding of the nation and forward to the present. Protesting a tax by dumping tea in the Boston Harbor was patriotic in the 18th century and this symbolic gesture resonated in the 20th century when the Internal Revenue Code was dumped into the Harbor. Many tie freedom from tax to liberty and to be anti-tax is seen as patriotic.<sup>25</sup> There is some evidence that an anti-establishment schema,

23. See, e.g., Kahan & Braman, *supra* note 14, at 153 (citing Mary Douglas and political scientist Aaron Wildavsky, *Risk and Culture* (1982)); Daniel W. Barrett, Wilhelmina Wosinska, Jonathan Butner, Petia Petrova, Malgorzata Gornik-Durose & Robert B. Cialdini, *Individual Differences in the Motivation to Comply across Cultures: The Impact of Social Obligation*, 37 *Personality and Individual Differences* 19 (2004).

24. See, e.g., Barrett, et al., *supra* note 23. Accord, Michael Wenzel, *An Analysis of Norm Processes in Tax Compliance*, 25 *J. Econ. Psychol.* 213, 222(2004) (finding that social norms that are internalized as personal norms positively affect compliance, but otherwise do not have a significant effect).

25. President Reagan, for example, on the signing of the Tax Reform Act of 1986, called the prior code “un-American” stating that “Throughout history, the oppressive hand of government has fallen most heavily on the economic life of the individuals. And, more often than not, it is inflation and taxes that have undermined livelihoods and constrained their freedoms.” President Reagan’s Remarks During Tax

perhaps more prevalent with those who have an anti-tax and/or individualistic view, is significantly related to tax compliance.<sup>26</sup> Like the anti-tax schema the anti-establishment schema – a Jeffersonian belief that small government is the best government – has deep roots in the American psyche. Logically, a person operating under this schema might support a small tax that pays for the small amount of necessary government. However, in practice, antipathy to government and antipathy to tax frequently accompany each other, especially if the tax and the government are larger than one prefers.

World views not only affect attitudes towards a substantive policy, but also affect responses to methods of enforcing the policy. A policy may be consistent with a person's world view, but the method of enforcement may not. Shaming is an example of such a policy. Recently, shaming has gained attention in several legal areas such as criminal law as an alternative to more traditional enforcement techniques such as imprisonment. It is also being used in the tax area. Several states, such as Alabama, California, North Carolina and Wisconsin have used shaming devices by publicizing the names of delinquent taxpayers. Even the Internal Revenue Code has a limited amount of shaming: section 6039G(d) publicizes in the federal register the names of taxpayers who expatriate for tax reasons.

In some situations, however, shaming sanctions may not only be ineffective but they may also backfire. They are ineffective on individuals who are not ashamed of their behavior and/or are not concerned for other reasons such as reputation that others know they have violated a compliance norm. Shaming may also be ineffective for a person who has internalized the norm but has an individualistic world view. Such a person will be hostile to shaming, which is based on a collectivist, communal world view, and that hostility may even undermine support for the underlying policy.<sup>27</sup>

People with different world views/cultural cognitions may have some social norms and personal norms that are the same, but others that differ. A

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Bill Signing Ceremony (Oct. 22, 1986) *reprinted* in 33 Tax Notes 413 (Oct. 27, 1986). See also, Excerpts from the President's 1988 Legislative and Administrative Message to Congress, 38 Tax Notes 499 (Feb. 1, 1988) ("If individuals are to possess genuine autonomy then they must be free to control their own resources, to enjoy the fruits of their labor, and to keep what they earn, free from excessive government taxation and spending."). See generally Marjorie E. Kornhauser, Legitimacy and the Right of Revolution: The Role of Tax Protests and Anti-Tax Rhetoric in America, 50 Buff. L. Rev. 819 (2002).

26. Trivedi, Shehata & Lynn, *supra* note 22, at 177, 187 (finding that a taxpayer's level of anti-establishment is statistically significantly related to tax compliance).

27. Dan M. Kahan has recanted his support of shaming in the criminal law area because of its divisive nature. Dan M. Kahan, What's Really Wrong with Shaming Sanctions (2006) SSRN 914503, at <http://papers.ssrn.com/abstract=914503>. (Arguing that sanctions, like the policies they enforce, must be devised in as ambiguous a way as possible so as to appeal to people with diverse world views; shaming is too divisive).

taxpayer with an individualistic world view, for example, is less likely to have egalitarian values than a collectivist. Both, however, may follow the same norm of procedural fairness. The next section examines some of the social norms and personal values that affect tax morale generally.

### *B. Social Norms and Personal Values*

Both social and personal norms affect tax morale. Social norms – shared beliefs concerning the manner in which people should behave – are enforced by informal social sanctions.<sup>28</sup> They are external to individuals whereas personal (moral, ethical) norms or values are internal. When a person internalizes a social norm, it becomes a personal one. Internalized personal norms are more likely to affect behavior in large groups, especially in situations where an individual's actions are not readily observable by others. Social norms are less influential in this type of situation because of the problems of free-riding and the difficulty of imposing sanctions.<sup>29</sup>

Some internal norms have strong positive impacts on tax compliance. Values indicating high moral reasoning – honesty and altruism, for example – provide internal rewards that can positively affect tax compliance.<sup>30</sup> A person may act on this personal norm regardless of what others are doing. However,

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28. See, e.g., Ivar Kolstad, *The Evolution of Social Norms: With Managerial Implications*, 36 *J. Socio-Econ.* 58 (2007). *Accord* Ernst Fehr & Urs Fischbacher, *Social Norms and Human Cooperation*, 8 *Trends in Cognitive Sciences* 185,185 (2004) (“Social norms are standards of behaviour that are based on widely shared beliefs how individual group members ought to behave in a given situation.”).

29. Studies show, for example, that people are more likely to recycle – an action that may not be easily observable or have much effect if others do not similarly recycle – if they believe it is good for the environment or a civic duty. See, e.g., Thomas C. Kinnaman, *Explaining the Growth in Municipal Recycling Programs: The Role of Market and Nonmarket Factors*, 152 in *The Economics of Household Garbage and Recycling Behavior* (Don Fullerton & Thomas C. Kinnaman eds, 2002) (respondents were more likely to participate in recycling if they believe that recycling was good for the environment than if they thought it was their civic duty); Ann E. Carlson, *Recycling Norms*, 89 *Cal. L. Rev.* 1231 (2001) (arguing that commitment to recycling influences recycling behavior but mostly in small groups requiring little effort); Georgina Davis, Paul S. Phillips, Adam D. Read & Yuki Iida, *Demonstrating the Need for the Development of Internal Research Capacity: Understanding Recycling Participation Using the Theory of Planned Behaviour in West Oxfordshire, UK*, 46 *Resources, Conservation and Recycling* 115 (2006) (finding that an intention to recycle influenced by belief that it was good for the environment).

30. See Nina Mazar & Dan Ariely, *Dishonesty in Everyday Life and Its Policy Implications*, 25 *Am. Marketing Ass'n* 117, 124 (2006); Trivedi, Shehata & Lynn, *supra* note 22, at 187 (an increase in the P Score – a measure of the level of moral reasoning – increased compliance while a decrease in the P score decreased compliance).

norms are not static; they interact with each other and with the environment.<sup>31</sup> For example, a taxpayer may initially follow her own personal norm of integrity and file accurate tax returns regardless of the social norm which tolerates cheating. However, the taxpayer's perception that others are cheating can influence her norms, lower tax morale, and change compliance behavior. Norms of conformity or reciprocity, for example, can alter her norm of integrity to justify some cheating as can the desire not to be seen as a "chump" who follows the law when everyone else doesn't.

Identification with the group plays a crucial role in norm formation and influence. The more a person identifies with a group, the more likely s/he is to internalize its norms and therefore cooperate, that is, follow them.<sup>32</sup> Some studies suggest that if a taxpayer does not identify with the group holding the social norm, the norm can actually negatively affect compliance.<sup>33</sup> However, even if a person does not identify with a group norm, s/he may comply with its norms for rational based reasons such as reputation. Compliance with laws "signals" that the person is trustworthy, honest or reliable.<sup>34</sup> For example, politicians engage in signaling when they open their tax returns to public scrutiny. Normally, however, signaling does not occur in the income tax context because tax returns are generally confidential.<sup>35</sup> Signaling would occur, however, if there were some publicity of tax information, such as publicizing the names of delinquent taxpayers.<sup>36</sup>

Identification with a group encourages individuals to be collectively oriented, and therefore, more likely to forgo immediate self interest for the sake of the public good. A taxpayer who is strongly identified with the group is more likely to see a tax not simply as coercion, but as "self-imposed levies, expressions of our commitment to the well-being of all."<sup>37</sup> In other words, identification with the group either decreases the importance of fiscal exchange

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31. Wenzel, *supra* note 24.

32. Tom R. Tyler, *Why People Obey the Law* (1990); Tom R. Tyler & Steven L. Blader, *The Group Engagement Model: Procedural Justice, Social Identity, and Cooperative Behavior*, 7 *Personality and Social Psychol. Rev.* 349, 355 (2003). Torgler makes the same point in many articles.

33. See, e.g., Wenzel, *supra* note 24.

34. Alex Raskolnikov, *Crime and Punishment in Taxation: Deceit, Deterrence, and the Self-adjusting Penalty*, 106 *Colum. L. Rev.* 569 (2006).

35. Dan M. Kahan, *Signaling or Reciprocating? A Response to Eric Posner's Law and Social Norms*, 36 *U. Rich. L. Rev.* 367, 378 (2003). But see Eric A. Posner, *Law and Social Norms: The Case of Tax Compliance*, 86 *Va. L. Rev.* 1781 (2000).

36. But see, Raskolnikov, *supra* note 34 (tax compliance as reputational signaling device) and Kahan, *supra* note 35 (reciprocity is better explanation of compliance). My conversation with Karl Knapp of the North Carolina Department of Revenue says there was anecdotal evidence that the mere threat of publication increased compliance. E-mail from Karl Knapp to author Mar. 2, 2007. This is some evidence that shaming could perform a signaling function.

37. Hansen, *Taxing Illusions* *supra* note 21, at 16.



– an element of procedural justice, as discussed below – or is more broadly defined to include others.

Identification with a group smaller than the nation also can positively influence internal motivations to comply with tax laws. If business leaders, for example, emphasize the importance of paying taxes (personally and at the corporate level), then other business-oriented people will see that as the norm. Similarly, having an important person in a group (a minister, for example) or a person that people admire or respect (e.g., celebrity) emphasize tax compliance could strengthen compliance.

Strengthening the identification of tax professionals with the integrity of the tax system can improve their willingness to cooperate with the IRS. This would decrease aggressive tax planning directly since much of such advice is “supply” driven by the professionals.<sup>38</sup> It would also signal to clients a tax compliance norm that could have a ripple affect on their clients, who respect and identify with these professionals.

A major reason people join groups and cooperate is because they obtain a sense of identity (self-worth, esteem) from the group.<sup>39</sup> Consequently the more one identifies with the group the more one internalizes norms and cooperates. Identification with the group is therefore crucial to cooperation and procedural fairness is crucial to forming that identification.<sup>40</sup>

Procedural fairness, or justice, is a major determinant of tax morale generally, not just in the fostering of identification. Key components of procedural justice are: voice<sup>41</sup> (participation in the process and belief authorities “hear” the individual); belief in the neutrality of the decision; belief in the neutrality of the decision-maker; and being treated with respect, politeness and dignity by tax authorities.<sup>42</sup> A belief in the legitimacy of the authority and trust in it, which a sense of procedural fairness augments, also increase identification with the group and compliance with its norms.

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38. John Braithwaite, *Markets in Vice: Markets In Virtue* 50-66 (2005); Dennis J. Ventry, Jr., *From Competition to Cooperation: Imagining a New Tax Compliance Norm* (2007 forthcoming).

39. Tyler & Blader, *supra* note 32, at 353.

40. E.g., *Id.* at 355.

41. See, e.g., Alm & Torgler, *supra* note 10, at 230; Feld & Frey, *supra* note 9, at 88-89; Benno Torgler, *Tax Morale and Direct Democracy*, 21 *Eur. J. Pol. Econ.* 525, 526-27 (2005).

42. See, e.g., Tom Tyler, *Why People Obey the Law* 71-74 (1990); Lars P. Feld & Bruno S. Frey, *Tax Compliance as the Result of a Psychological Tax Contract: The Role of Incentives and Responsive Regulation*, 29 *Law & Pol’y* 102, 104 (2007); Torgler, *supra* note 2, at 676; Tyler & Blader, *supra* note 32; Tom R. Tyler & David De Cremer, *Process-based Leadership: Fair Procedures and Reactions to Organizational Change*, 16 *Leadership Q.* 529, 542 (2005); Tom R. Tyler, *Promoting Employee Policy Adherence and Rule Following in Work Settings*, 70 *Brook. L. Rev.* 1287, 1310 (2005).

Although a belief in the legitimacy of the tax system is ultimately tied to the greater issue of legitimacy of the government which the taxes support, individuals' direct contacts with the tax authority greatly influence their perception of whether an authority is legitimate and procedurally fair.<sup>43</sup> The more an individual believes s/he is heard and treated fairly, the more s/he believes the authority is responsive and therefore procedurally just.<sup>44</sup> The lack of responsiveness, according to some scholars, is a major cause of the ultimate act of non-compliance in the tax area – revolt.<sup>45</sup>

Procedural justice builds trust, loyalty, identification, and commitment that can survive the occasional negative interaction with the authority. Commercial companies, for example, devise complaint procedures which preserve customer loyalty even in the face of negative experiences.<sup>46</sup> Procedural justice can work similarly in the tax context. By strengthening normative bonds,

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43. See, e.g., Natalie Taylor, *Explaining Taxpayer Non-Compliance through Reference to taxpayer Identities: A Social Identity Perspective* 39, 51 in *Size, Causes and Consequences of the Underground Economy: An International Perspective* (Christopher Bajada & Friedrich Schneider eds. 2005).

44. See, e.g., Kent W. Smith, *Reciprocity and Fairness: Positive Incentives for Tax Compliance* 223, 228 in *Why People Pay Taxes* (Joel Slemrod ed., 1992)(although procedural justice and responsiveness are different, “the two components may be cumulative in such regulatory areas as tax administration, in the sense that responsive service may be viewed by many as a precondition for procedural fairness in decision making and the administration of the laws.” Therefore, it is “reasonable to expect that perceptions of pf are an intervening variable between perceptions of responsive service and normative commitment.”). Kent also highlights the (probable) importance of reciprocity and legitimacy.

45. See, e.g., Jack Citrin, *Introduction* at 19 in *California and the American Tax Revolt: Proposition 13 Five Years Later* (Terry Schwadron, Ed; Paul Richter, Principal writer 1984), (“a failure on the part of elected officials to meet burgeoning complaints about high taxes at least partway was critical to the success of the tax revolt. The rebels won their greatest victories, in California and Massachusetts, where the political system was unresponsive to an obvious problem – in other words, where democratic processes broke down.”). Lack of responsiveness by officials also played an important role in other tax revolts in the United States such as Shays' Rebellion and the Whiskey Rebellion. See Kornhauser, *supra* note 25.

46. Consumer research indicates that in order to build a long-lasting connection between a customer and a brand, the customer must be “committed” to the brand. This relationship exceeds the usual “brand loyalty” marketers discuss; loyalty is functional, arising from satisfaction with the brand whereas commitment is personal and based, in the consumer's trust in the brand. A committed customer is “slightly more forgiving of the brands foible since the relationship has escaped the limitations of a straightforwardly utilitarian nature.” Jeff Hess & John Story, *Trust-based Commitment: Multidimensional Consumer-brand Relationships*, 22 *J. Consumer Marketing* 312, 321 (2005). See, also, Hooman Estalami, *Competitive and Procedural Determinants of Delight and Disappointment in Consumer Complaint Outcomes*, 2 *J. Service Res.* 285, 289 (2000)(promptness, politeness and empathy improve commitment).

it can help maintain compliance even in the face of important negatives such as fiscal exchange inequities, IRS mistakes, or taxpayer complaints. Theoretically, certain existing structural aspects of the tax process, such as the taxpayer bill of rights and the National Taxpayer Advocate, should have a positive effect on compliance. The more the IRS strengthens its own norms of honesty, fairness, and politeness in its communications and interactions with taxpayers, the more taxpayers will view the IRS and its decisions as fair.<sup>47</sup> This increased perception of procedural justice should improve tax morale and tax compliance.

The norm of reciprocity, like procedural justice, improves tax morale. Acting under this norm an individual will respond to another's act in the same way in which that person treated him.<sup>48</sup> If another person is generous or honest, for example, the individual feels obligated to respond in kind and is more likely to do so. However, if the other person acts negatively – such as cheats or shirks – the individual will respond in a similarly negative fashion. Acting under a norm of reciprocity, a person may voluntarily comply with tax laws even if s/he does not personally experience fiscal equity in the tax/government benefit exchange because s/he is helping the collective good. Strong norms of reciprocity, therefore, increase cooperative behavior. Reciprocity and cooperation increase when people trust that others will indeed reciprocate.

Several studies indicate that trust and reciprocity hold true in the tax area as well as generally. An individual taxpayer's compliance after the Tax Reform Act of 1986 correlated, according to one study, with exposure to other taxpayers' positive attitudes to the act, rather than the amount of personal benefit from the reforms (i.e. decreased taxes).<sup>49</sup> Positive attitudes indicated greater willingness to comply, which in turn "trigger[ed] the disposition to reciprocate in kind. In effect, the enactment of popular reforms generates an environment of face-to-face assurance giving that builds trust, and a resulting disposition to cooperate, in much the same way that discussion does in public goods experiments."<sup>50</sup> Learning that most people pay their taxes can similarly reinforce trust and reciprocity.<sup>51</sup>

Reciprocity theory implies that a very effective method of promoting cooperative behavior is "to promote *trust* – the shared belief that others can in fact be counted on to contribute their fair share to public goods, whether or not

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47. Organizations also have norms which, like individual norms, can be changed. Kolstad, *supra* note 28; Tyler & De Cremer, *supra* note 42 (leaders can motivate others in the organization to accept change through fair procedures).

48. See, e.g., Dan M. Kahan, *Logic of Reciprocity*, 102 Mich. L. Rev. 71 (2003); Kahan Posner Response, *supra* note 35; Dan M. Kahan, *Trust, Collective Action, and Law*, 81 B.U. L. Rev. 333, 333 (2001) (hereinafter Kahan Trust).

49. Kahan Trust, *supra* note 48, at 341, citing Marco R. Steenbergen et al., *Taxpayer Adaptation to the 1986 Tax Reform Act: Do New Tax Laws Affect the Way Taxpayers Think About Taxes?*, in *Why People Pay Taxes* 9 (Joel Slemrod, ed., 1992).

50. Kahan Trust, *supra* note 48, at 343.

51. See Kahan *supra* note 35 at 379.

doing so is in their material self-interest.”<sup>52</sup> The best ways to promote trust is to promote procedural justice, legitimacy, and identification.

*C. Impact of External Factors on Internal Motivations*

Although tax morale is internally motivated, the outside world affects it. Some external factors – such as contextual clues, rewards, education, and the framing of communications – can weaken (“crowd-out”) internal motivators while other external factors strengthen (“crowd-in”) internal motivations. IRS actions may have either effect – often unintentionally. By understanding the workings of tax morale, the IRS can maximize positive effects and minimize those that crowd out tax morale.

The commoditization of a behavior crowds out positive normative influences on that behavior. Thus, setting a price or giving an economic incentive for behavior motivated by social, non-pecuniary motives such as reciprocity can actually decrease the desired behavior. In the environmental field, for example, subsidies, some argue, crowd out normative behaviors.<sup>53</sup> In tax, it is possible that commodification occurs when taxpayers are called “customers.” The effects of crowding out can be permanent so that decreased compliance remains even after the discontinuance of the economic incentive or other commoditizing event.<sup>54</sup>

The manner in which a communication is framed can either activate or suppress internally motivated normative behavior. In one experiment, subjects received \$18. Half the group was told that \$2 had been given to a charity of their choice; the other half was told that they had been given \$20 but the government had taken \$2 in taxes which was then given to the charity of their choice.<sup>55</sup> When asked if they wanted to make additional charitable contributions, those that had been “taxed” did not, but those subjects who had simply been told \$2 had gone to charity contributed more.<sup>56</sup> Although neither group had a choice whether to give the initial \$2, the “tax” situation highlighted the compulsory aspect (or alternatively framed the situation as a loss situation

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52. *Id.* at 369.

53. Andrew Green, *You Can’t Pay Them Enough Subsidies: Environmental Law and Social Norms*, 30 *Harv. Envtl. L. Rev.* 407 (2006)(subsidies put a price on environmental behavior and crowd out behavior based on responsibility). But see, Carlson, *supra* note 29, at 1297 (market mechanisms do decrease “bad” recycling behavior and increase “good” behavior).

54. Fehr & Falk, *supra* note 4, at 713-18.

55. *Id.* at 1548-57.

56. *Id.* Catherine C. Eckel, Philip J. Grossman & Rachel M. Johnston, *An Experimental Test of the Crowding Out Hypothesis*, 89 *J. Pub. Econ.* 1543, (2005).

since \$2 of their money had been taken from them).<sup>57</sup> This crowded out the voluntary charitable behavior.<sup>58</sup>

Phrasing norms positively generally encourages or activates normative behavior (at least for women). For example, stating that most people comply with tax laws reminds people what the norm is and encourages them to follow it. This crowding in effect may be due to the effect of conformity and reciprocity norms. On the other hand, framing communications negatively, by emphasizing the number of people who violate the norm, crowds out normative behavior. For example, theft of petrified wood at the Petrified Forest National Park decreased when a sign – with a line through it – showed only one person stealing wood as opposed to three.<sup>59</sup> When college students are told that the average student consumes 4 drinks on a Saturday night, those who consume more decrease their drinking, but those who drink less than 4 increase their consumption.<sup>60</sup> Similarly, communications stating how many people are evading taxes might decrease compliance among formerly compliant taxpayers because their perception about the strength of the norm and how many taxpayers follow it (reciprocity) diminishes.

Laws can influence behavior and activate personal norms in various ways. “Expressive” provisions, such as shaming, signal socially approved behavior, as well as increase the costs (penalties) of disapproved behavior. They, therefore, have the potential to shape social norms and increase compliance.<sup>61</sup> They work best, however, if individuals identify with the group and have a similar world view, as discussed previously. Consequently, shaming, a technique with which several states are experimenting by publicize tax delinquents, may not only be ineffective for those who do not identify with the norm (paying taxes), but may backfire and indicate to those who are compliant that the norm is not followed by many people.<sup>62</sup>

Crowding-in can occur through internal rewards. For example, being treated respectfully – an aspect of procedural fairness – can activate internal motivations.<sup>63</sup> Moreover, seeing examples of the desired behavior can activate

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57. *Id.*

58. *Id.* at 1557.

59. Robert B. Cialdini, *Descriptive Social Norms as Underappreciated Sources of Social Control*, 72 *Psychometrika* 263, 266 (2007) (arguing theft actually increased when the sign showed 3 thieves).

60. Robert B. Cialdini, talk at ASU College of Law (January 29, 2007).

61. See Michael S. Kirsch, *Alternative Sanctions and the Federal Tax Law: Symbols, Shaming, and Social Norm Management as a Substitute for Effective Tax Policy*, 89 *Iowa L. Rev.* 863 (2004). Politics itself can be seen as symbolic. For the classic exposition of this theory see, Murray Edelman, *The Symbolic Uses of Politics* (1964).

62. See *supra* notes 27 and 58 and accompanying text, regarding ineffectiveness of shaming.

63. See, e.g., Feld & Frey, *supra* note 42 at 105-06.

a person's norms. For example, when people hear, see, or read about polite behavior, they will act more politely,<sup>64</sup> or they will donate more to a box in the museum if the box already has money in it.<sup>65</sup> These external cues activate the norm of reciprocity or perhaps the norm of conformity in which people act as others do even though there is no chance of receiving a reciprocal benefit.<sup>66</sup>

Several opportunities to provide external cues to activate tax compliance norms occur at the time returns are filed. For example, Mazar and Ariely suggest that the IRS could ask taxpayers to sign an "honor code" just before they fill out their returns.<sup>67</sup> Cialdini suggested that taxpayers be given the opportunity on their tax form to contribute a nominal sum to fighting tax evasion.<sup>68</sup> Such a fund is framed negatively and therefore might backfire and decrease compliance, but the idea, framed more positively, is intriguing. For example, the contribution could be to fund IRS tax advice to the public or a segment of the public (such as the poor) or to fund special tax education programs. Another possibility, borrowed from campaigns to get out the vote at election time, is to provide taxpayers with stickers that say "I paid my taxes today." This visible sign of compliance might activate norms of reciprocity and trust that would encourage others to similarly pay their taxes.

Education can strengthen norms. Since norms and morality are acquired through a process of socialization, education can strengthen norms that are positively correlated with tax compliance such as honesty, morality, national pride, concern for others, and fairness.<sup>69</sup> Policy makers and administrators can develop programs that not only provide tax information but also "reinforce the concept of fairness of the tax system among tax payers; and develop programs

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64. E.g., Malcolm Gladwell, *Blink: The Power of Thinking Without Thinking* 25 (2005).

65. Frey & Torgler, *supra* note 3.

66. Nicholas Bardsley & Rupert Sausgruber, *Conformity and Reciprocity in Public Good Provision*, 26 *J. Econ. Psychol.* 664 (2005).

67. See Mazar & Ariely, *supra* note 30.

68. Cialdini, *supra* note 8. The federal government currently allows taxpayers to contribute to the Federal election campaigns and some states allow taxpayers to contribute to various funds.

69. See, e.g., Mazar & Ariely, *supra* note 30 at 123 (asserting "likely possibility" that critical period for developing these norms is in youth); Trivedi, Shehata & Lynn *supra* note 22, at 193 Policymakers, . . . should develop programs that help enhance these characteristics in the general population to raise the level of tax compliance. Encouraging education can be one such measure, given the finding in prior research that education and age are the most important determinants of moral reasoning. Thus, education with an emphasis on ethics, and the ethics of taxation specifically, may improve tax compliance. Furthermore, the results also highlight the importance of encouraging and maintaining a positive attitude towards governments amongst the general population to achieve a tax compliant population. Thus, policies that encourage/emphasize education and ethical behavior may be an effective method of increasing the level of taxpayers' compliance." *Id.* (Citation omitted).

that enhance and appeal to a taxpayer's moral conscience and reinforce social cohesion."<sup>70</sup>

Although it is clear that external factors can activate or suppress tax morale, laboratory studies and field experiments with actual taxpayers produce mixed results regarding normative appeals to pay taxes.<sup>71</sup> Some studies show no impact or even a negative one. These results, however, do not necessarily mean that external factors cannot activate norms. Peculiarities of the studies themselves may be the cause. For example, the normative appeal may fail because there was too long a time lag between the communication and the compliance decision, or because the communication was a "one-shot" deal or was not framed properly.<sup>72</sup> Moreover, as discussed below, normative appeals appear to work better with some segments of the population than other segments.

#### *D. Demographic Factors*

Various demographic factors correlate with tax compliance behavior, such as age, gender, and religiosity. These are correlations not causations and may reflect different world views, schemas, framing, or a combination of these. Although the precise reasons for the correlations are not known, knowledge that they exist is useful in devising compliance tactics. What helps one population may be a detriment to another. Studies have found these major demographic correlations:

*Gender:* Although some of the study results are mixed, in general the evidence suggests that women are more compliant than men (perhaps because they are more risk averse), respond better to positive appeals (whereas men respond better to negative ones) and respond better to normative appeals.<sup>73</sup>

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70. Trivedi, Shehata & Lynn, *supra* note 22, at 175.

71. E.g. See. For example, various studies of effect of letters sent to Minnesota taxpayers: Marsha Blumenthal, Charles Christian & Joel Slemrod, Do Normative Appeals Affect Tax Compliance? Evidence from a Controlled Experiment in Minnesota, (2001) 54 Nat'l Tax J. 125; Jon Hasseldine, Peggy A. Hite, Simon James & Marika Toumi, Carrots, Sticks, Sole Proprietors, and Tax Accountants, Recent Research in Tax Administration and Compliance, Proceedings of the 2005 IRS Research Conference 191(2006); Joel Slemrod, Marsha Blumenthal, Charles Christian, Taxpayer Response to an Increased Probability of Audit: Evidence from a Controlled Experiment in Minnesota, 79 J. Pub. Econ. 455 (2001).

72. See, e.g., Blumenthal, Christian & Slemrod, *supra* note 71, at 135.

73. E.g., Cullis, Jones & Lewis, *supra* note 18 at 315 (study of UK college students showed male students declared less income when the question was framed as a loss); Janne Chung & Viswanath Umashanker Trivedi, The Effect of Friendly Persuasion and Gender on Tax Compliance Behavior, 47 J. Bus. Ethics 133 (2003); Klarita Gerxhani & Arthur Schram, Tax evasion and Income Source: A Comparative Experimental Study, J. Econ. Psychol. 27 402 (2006); John Hasseldine & Peggy A. Hite,

*Age:* Older individuals are generally more compliant than younger ones.<sup>74</sup> This could be due to a variety of factors such as older individuals have more social capital (more willing to follow or internalize social norms), have more at risk, and/or have more knowledge of tax.

*Education:* Findings regarding the correlation of education and compliance have been mixed.<sup>75</sup> As with other factors, however, mixed findings may be the product of the measurement tools – both how compliance is defined and education measured. Education may correlate with compliance because the internalization of social norms occurs through a process of socialization and education influences that process.<sup>76</sup> Education may also correlate with compliance because higher moral reasoning positively correlates and higher moral reasoning can be taught.

*Marital status:* Findings regarding the effect of marital status are mixed.<sup>77</sup>

*Religion:* A study of the correlation between tax compliance and religion in more than thirty countries, found a positive correlation for all the main religions but found different correlations with different religions. For example, agreeing with an earlier study, Torgler found that those with a strong

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Framing, Gender, and Tax Compliance, 24 J. Econ. Psychol. 517, 521 (2003); Robert W. McGee & Michael Tyler, Tax Evasion and Ethics: A Demographic Study of 33 Countries, SSRN abstract #940505 (Oct. 2006) (arguing women more likely to oppose tax evasion than men); Benno Torgler, Tax Morale and Tax Compliance A Cross-Culture Comparison, National Tax Assoc. Annual Proceedings 96th Annual Conference 2003, 63, 71 (females report a higher compliance than males).

74. See, e.g., McGee & Tyler, *supra* note 73 (finding that older people tend to be more opposed to tax evasion than younger people); Benno Torgler, The Importance of Faith: Tax Morale and Religiosity. 61 J. Econ. Behav. & Org. 81, 87-88 (2006) (using data from the WVS 1995-7 for more than 30 countries at individual level). But see, Torgler & Schneider, *supra* note 5 (arguing after age 64 tax compliance decreases).

75. Torgler, *supra* note 73 (arguing education has a positive effect on tax compliance.); but see, McGee & Tyler, *supra* note 73 (less well educated more opposed to evasion). Kirchler, et al., *supra* note 6 at 514 (Willingness to cooperate – measured by intent to file correct, timely tax returns – was significantly related to higher self reported tax knowledge. “Several studies using education as a proxy for knowledge or measuring objective or subjective knowledge confirm the positive relationship between knowledge and willingness to cooperate or comply [.]” *Id.* (Citation omitted).

76. Mazar & Ariely, *supra* note 30.

77. Torgler, *supra* note 74, at 94 (singles had lower compliance than married couples and those living together); Andreoni et al., *supra* note 2, at 840 (TCMP found greater noncompliance among married couples).



protestant work ethic were more likely to oppose taxation.<sup>78</sup> The correlation may exist because religion acts as a “supernatural police”<sup>79</sup> or because it is a proxy for such traits as work ethic and trust.

*Income:* The evidence regarding the correlation between income and compliance is mixed.<sup>80</sup>

#### *E. Using Tax Morale to Increase Compliance*

Recently several tax authorities have switched their approach to tax administration from a one-size-fits-all enforcement model to a model that builds on the lessons of tax morale research. Frequently called a self-regulatory or responsive regulation model, this model adopts “carrots,” as well as “sticks,” in a manner that matches the tax authority’s response to that of the regulated individuals (taxpayers), saving the sticks for those who are non-compliant. The Australian Taxation Office (ATO) has been the leader in responsive regulation in the tax field. This model has now been adopted by other countries (UK, New Zealand, Timor Lese, Indonesia and the state of Pennsylvania).<sup>81</sup>

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78. Torgler, *supra* note 74, *The Importance of Faith: Tax Morale and Religiosity*, 61 *J. Of Economic Behavior & Organization* 81, 91 (2006). Accord Benno Torgler, *To Evade Taxes or Not to Evade: That Is the Question*, 32 *J. Socio-Econ.* 283 (2003)

(“ . . . Strong evidence has been found that trust in government, [national] pride, and religiosity have a systematic positive influence on tax morale. . . [and] [t]his effect tends to persist even after controlling for age, income, education, gender, marital status, employment status.”)

79. Torgler & Schneider, *supra* note 5, at 10.

80. Gërkhani & Schram, *supra* note 73 (compliance increases with higher income); Torgler, *supra* note 73. But see McGee & Tyler, *supra* note 73 (poorer are more opposed to evasion than wealthier, but authors are skeptical of result).

81. The Australian Taxation Office and Australian researchers have been leaders in responsive regulation from a tax standpoint. See e.g., Australian Taxation Office at <http://www.ato.gov.au/> and Centre for Tax System Integrity at <http://ctsi.anu.edu.au/index.html>; See generally Valerie Braithwaite, *Responsive Regulation and Taxation: Introduction*, 29 *Law & Pol’y* 1 (2007); See also, John Braithwaite, *supra* note 38; Valerie Braithwaite, *Dancing with Authorities*, in *Taxing Democracy: Understanding Tax Avoidance and Evasion* (Valerie Braithwaite ed., 2003); Sagit Leviner, *A New Era of Tax Enforcement: From ‘Big Stick’ to Responsive Regulation* at <http://ssrn.com/abstract=940911>; Tony Morris & Michele Lonsdale, *Translating the Compliance Model in to Practical Reality*, the *IRS Res. Bull.: Recent Research on Tax Administration and Compliance*, Pub. No. 1500, 57, 59 (2005) (New Zealand BISEP – Business; Industry; Sociological; Economical; Psychological). Kristina Murphy, *The Role of Trust in Nurturing Compliance: A Study of Accused Tax Avoiders* 8 *Law & Human Behav.* 187 (2004) (one of the first papers to provide empirical evidence to support a regulatory strategy based on trust); Kathleen Carley & Daniel T. Maxwell, *Understanding Taxpayer Behavior and Assessing Potential IRS*

Valerie Braithwaite, a leading researcher in the field, describes the responsive regulation, or “tax morale,” model – at least as currently practiced by the ATO – as follows:

[Responsive regulation] . . . refers to the practice of (a) influencing the flow of events (b) through systematic, fairly directed and fully explained disapproval (c) that is respectful of regulatees, helpful in filling information gaps and attentive to opposing or resisting arguments, (d) yet firm in administering sanctions (e) that will escalate in intensity in response to the absence of genuine effort on the part of the regulatee to meet the required standards. Responsive regulation . . . deliberates on shared community goals and understandings, it enforces agreed upon standards, preferably through teaching, persuading and encouraging those who fall short, but it uses punishment when necessary to achieve its regulatory objectives.”<sup>82</sup>

The core of responsive regulation is the dynamic partnership it creates between the tax authority and the taxpayer. It encourages taxpayers to “think about their obligations and accept responsibility for regulating themselves in a manner that is consistent with the law” and the tax authority agrees to respond appropriately.<sup>83</sup> Recently, Feld and Frey have extended the ATO tax morale based model by proposing a “psychological tax contract” which includes positive rewards for compliant taxpayers in a manner that does not undermine internal motivations to comply.<sup>84</sup> Since the psychological contract is premised on the idea of improving tax morale, especially by means of fair procedures and respectful treatment (in other words, procedural justice), it rewards – rather than punishes – taxpayers. The authors broadly conceive “reward” to extend beyond the traditional fiscal exchange of receiving material goods and services for taxes – which, in fact, commoditize taxes – to include “the political procedures that lead to this exchange . . . and the personal relationship between the taxpayers

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Interventions Using Multiagent Dynamic-Network Simulation, the IRS Res. Bull.: Recent Research on Tax Administration and Compliance, Pub. No. 1500, 93 (2006) at <http://www.irs.gov/pub/irs-soi/06carley.pdf>.

82. Valerie Braithwaite, *Responsive Regulation and Taxation: Introduction*, 29 *Law & Pol’y* 1, 5 (2007); see also J. Braithwaite, *supra* note 38, at 71 (four “prongs of the ATO Compliance Model are: (a) Understanding taxpayer behavior; (b) Building community partnerships; (c) Increased flexibility in ATO operations to encourage and support compliance; and (d) More and escalating regulatory options to enforce compliance”).

83. V. Braithwaite, *supra* note 81, at 6.

84. Feld & Frey, *supra* note 42, at 104-05.

and the tax administrators.”<sup>85</sup> Although their model applies traditional deterrence when necessary, the authors believe that because “genuinely rewarding taxpayers in an exchange relationship will increase tax compliance, [i]t should thus be considered as the tax authority’s dominant strategy to approach taxpayers in order to enhance their tax compliance, while at the same time being able to resort to punishment if that strategy fails.”<sup>86</sup>

The responsive regulation model is a positive step towards improving tax compliance by recognizing internally motivated tax morale factors and the role of the tax authority in promoting them. Nevertheless, this model poses several problems. First, a tax authority following the model must navigate a narrow strait between Scylla and Charbydis: being too lenient (or soft) and being too hard – both of which can decrease tax compliance by eroding tax morale. Moreover, a flexible system, necessary for responsive regulation to work, can also decrease tax morale if the necessary discretion creates arbitrary decisions that undermine a sense of procedural fairness. Several commentators have suggested that the way to avoid both problems is through “institutional integrity” which goes beyond “mere procedure” to encompass “the whole matrix of values, purposes and sensibilities that should inform a course of conduct.”<sup>87</sup> Authorities must not only deal fairly with taxpayers but effectively – authorities must conduct themselves in a manner that appears both competent and honest, using procedures that taxpayers view as sensible and efficient.<sup>88</sup> This will require both training and diligence on the part of the taxing authority.

Another problem of the ATO model is that it does not require the tax authority to know the actual attitudes and motivations of the taxpayer. It assumes that taxpayer attitudes/motivations are reflected in their behavior, and it responds according to that behavior.<sup>89</sup> This assumption, however, is not always true. First, attitudes do not always translate into behavior. Consequently, it is still important for the taxing authority to understand the attitudes and motivations of its taxpayers in order to transform positive attitudes into positive actions and not crowd-out these positive attitudes. Moreover, since different attitudes and motivations may produce the same behavior, the more the tax authority understands about actual attitudes and motivations, the more it can respond accurately and positively to taxpayers. That is, if taxpayer B complies because of a social norm that people should comply and taxpayer C complies because of deterrents such as penalties, the same IRS action (e.g., publishing statistics regarding rate of convictions) may affect the two taxpayers’ behavior

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85. *Id.* at 115.

86. *Id.* at 116.

87. Vivienne Waller, *The Challenge of Institutional Integrity in Responsive Regulation: Field Inspections by the Australian Taxation Office*, 29 *Law & Pol’y* 67, 69 (2007) (citing Philip Selznick, *The Moral Commonwealth: Social Theory and the Promise of Community* 333 (1992)).

88. See, e.g., *id.*

89. See, e.g., Leviner, *supra* note 81.

differently. Taxpayer B may decrease her compliance whereas as taxpayer C might increase his compliance.

Mark Burton argues that another problematic aspect of responsive regulation is that tax law – contrary to the model’s premise – is not wholly determinate.<sup>90</sup> Since people disagree as to what the law is, it is difficult to agree on mutual goals, the proper interpretation of laws (or who is the proper interpreter), or to form partnerships to achieve them.

#### *F. Summary of Tax Morale Literature*

Tax morale research, a subset of general research into why people obey laws, has made great strides in understanding tax compliance, but much is still to be learned. It has identified key components of tax morale such as procedural fairness, trust, legitimacy, identification with the group, and reciprocity. It has also identified key mental and affective factors influencing tax morale – such as framing issues – and has begun isolating ways in which external factors can encourage or depress tax morale. Although research has yielded much information, much is still to be learned. Further research will help explain some of the conflicting results in empirical research and provide better guidance for tax agencies to improve compliance.

Although tax morale is a work in progress, enough is known to suggest that tax authorities abandon traditional regulatory models that focus solely on one-size-fits-all enforcement and adopt a “tax morale” model. Several countries, such as Australia, have already done so. Although the tax morale model uses traditional enforcement mechanisms such as fines and audits, it emphasizes taxpayers’ internal motivations – social norms, personal values, and cognitive processes. Recognizing that external factors – including actions by the tax authority – can affect norms and values in either positive or negative ways, a tax morale-based tax authority abandons a one-size-fits-all approach to taxpayers and develops more individualized methods to match the differing attitudes and behaviors of different types of taxpayers.

Current tax morale models, such as the ATO’s, are a step forward in improving tax compliance, but they do have several limitations. First, they can be vague as to exact implementation. Second, the model’s flexibility in dealing with taxpayers, which is an advantage, is also a potential disadvantage in that it may lead to inconsistent administrative response. Third, it has the potential of backfiring and lowering tax morale (and compliance) because inconsistent administrative responses may impair the taxpayer’s sense of procedural fairness. Similarly, the taxpayer may lose trust in the tax agency if it views the agency’s actions to improve morale as manipulative.

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90. Mark Burton, *Responsive Regulation and the Uncertainty of Tax Law – Time to Reconsider the Commissioner’s Model of Cooperative Compliance?*, 5 *Journal of Tax Research* 71, 73 (2007).

A tax morale model can work only as well as the tax agency's understanding of the attitudes and behaviors (always recognizing that the two are not the same) of both compliant and non-compliant taxpayers so that the former may be strengthened and the latter changed. In order to do this, the agency must research tax morale and develop strategies and programs that apply current and future findings to taxpayers and to its own personnel and procedures. The following Part IV recommends the establishment of a structure within the IRS to perform this function and provides some specific recommendations based on existing findings.

#### IV. RECOMMENDATIONS

The application of tax morale research to the formulation of tax laws and their application by the IRS must be an essential part of any successful plan to narrow the tax gap and improve and maintain taxpayer compliance. The findings have broad applicability for Congress and the IRS: They can help shape both laws and procedures; they can apply to both carrots (incentives) and sticks (enforcement/penalties), and they are relevant for all types of taxpayers. These recommendations, however, focus only on the IRS, only positive incentives, and only on individual taxpayers.

This Report makes three major recommendations and several specific suggestions. The three major recommendations are:

1. The IRS should establish a permanent department or other structure within its organization devoted solely to voluntary compliance issues. Although this structure should address all type of taxpayers, these recommendations cover only individual taxpayers. This Report labels the structure the Behavioral Science Unit (BSU).
2. The IRS should adopt a "tax morale" model of compliance that incorporates internal taxpayer motivations and emphasizes a more individualized carrot and stick approach than traditional tax collection models.
3. The IRS should implement long- and short-term educational and media programs to encourage voluntary compliance that incorporate the findings of behavioral research.

The first three sections of this Part describe the major recommendations generally. The final section suggests several more particular topics to be explored or implemented by the BSU. Although some recommendations can be broadly phrased and have widespread effects, there can be no one-size-fits-all recommendation that will improve all taxpayer compliance. Since the amounts,

types, and causes of individual noncompliance are so varied, some recommendations can only target certain types of noncompliance.

#### *A. Establish a Behavioral Science Unit*

##### *1. Scope*

Although the BSU derives its name from a similarly named unit within Her Majesty's Revenue and Customs (HMRC), this Report envisions a broader scope than that currently engaged in by the British unit. Ideally, the BSU should encompass many functions, such as evaluating third party research, conducting its own independent research, advising other parts of the IRS, and helping implement research findings. Whatever its scope, for maximum effectiveness, the BSU should be a permanent feature of the IRS with resources and personnel dedicated to compliance issues. Compliance involves many disciplines and many types of tasks such as research, developing IRS procedures and strategies; educating the public; and educating and training IRS officials. Although behavioral research can enhance both the positive (carrot) and negative (stick) tools which the IRS needs for compliance, these recommendations focus on the positive aspects. The next sections sketch a description of the types of personnel the BSU should hire and the functions it should perform.

##### *2. Personnel*

Ideally, a full-time director should head a full-time staff composed of persons with expertise in a variety of fields such as economics (especially behavioral economics), psychology, sociology, education, marketing, and even moral philosophy. The multi-disciplinary approach serves a dual function. First, it increases the breadth, depth, and sophistication of expertise since different fields have different strengths and perspectives. The multi-disciplinary approach, however, also increases the chance that other IRS personnel will accept the findings and assistance of the BSU since different people value different disciplines.<sup>91</sup>

The BSU should also hire outside consultants, when necessary, to perform a variety of functions such as research or designing educational and marketing campaigns. Many projects will require collaboration not just with IRS officials outside the BSU, but with people in other disciplines as well as other government, private, and non-profit organizations – and the public generally.

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91. Interviews with various personnel at HM Revenue and Customs (London, May 23, 2007) (importance of hiring non-economists as well as economists because some people are suspicious of, or uncomfortable with, economics).

Given the diversity of tasks, the staff as a whole should have theoretical, empirical, and practical capabilities. Some people must be able to design or evaluate empirical studies; others must be able to design (or help design in conjunction with outside experts) educational and training materials; still others must have the interpersonal skills to interface with people within the IRS and with the general public, as well as other agencies.

### *3. Functions*

The BSU ideally should perform many functions including research, analysis, advising the IRS, education, and training. Some of this work may be initiated by the BSU itself while other projects may be contracted for by other portions of the IRS in the furtherance of some strategy or procedure it is developing. The following sections generally describe some of these functions. The final section of this Part suggests some more particular areas of inquiry, but many more exist or will develop as research continues.

#### *a. Research and Analysis*

Knowledge in motivational and behavioral aspects of taxpayer compliance draws from a variety of fields including law, psychology, political science, and economics. Some of this research is specific to tax; other research deals with laws that have similar compliance issues, such as recycling, while some concerns compliance generally – such as research regarding the role of shaming. Still other research is not directly related to law but is relevant to tax compliance because it involves cognitive behavior generally, such as education (how people learn), political science (what makes people vote for certain candidates/policies), moral philosophy/reasoning (stages of moral reasoning), and marketing/advertising, (issues of vital concern to tax: framing, trust, and loyalty).

The BSU should perform original research, evaluate research of others, and also apply that research, creating practical solutions to compliance problems. Its personnel should engage in a variety of research tasks including reading existing theoretical and empirical studies; consulting with tax authorities in other developed countries; and conducting empirical studies. The latter, which might be done in conjunction with outside consultants, should draw on both the vast amount of data the IRS possesses as well as using knowledge garnered from existing literature. It should help other IRS units evaluate their problems, suggest appropriate research, and help translate that research.

Empirical studies should extend beyond laboratory and survey experiments to include developing new methods to increasing compliance. This task involves designing and executing field studies with actual taxpayers, such

as those done in Minnesota, or in Australia.<sup>92</sup> As the BSU gains more experience and knowledge, more of its efforts should be devoted to implementing its findings; designing and conducting these experimental studies would be a first step towards doing so. These trial experiments should cover all aspects of compliance such as designing forms, procedures for personnel, and educational material.

*b. Educational/Training Component*

Although tax morale has strong affective components, education can still play a major role in maintaining and improving compliance. Knowledge increases taxpayers' sense of control of their tax situation and also increases the chances of filing accurate and timely returns. Consequently, knowledge can decrease feelings of frustration as well as decrease the actual amount of time a taxpayer must spend on taxes. Education is also a powerful tool for increasing taxpayer morale by strengthening feelings of identity, reciprocity, fairness, procedural justice. Furthermore, education can ensure that IRS personnel act – and are perceived as acting – in a fair manner which is essential for tax morale.

In light of education's importance, the BSU must be involved in both internal and external education to meet the varying needs of taxpayers and personnel. Internal education includes revising IRS procedures and forms; training IRS personnel in behaviors that increase compliance, and developing recommendations for Congress. External education spans a vast spectrum of long-term and short-term educational programs for all ages of people, from children to the elderly, and all types of taxpayers – from unsophisticated individuals to tax preparers.

The IRS needs a range of educational programs to meet the various needs of taxpayers. Different portions of the population not only have different learning styles, but different tax issues, different psychological motivations, and differing social norms. The BSU should develop some of these programs in cooperation with other institutions. For example, it could partner with university departments such as an education department to design curriculum or it could work with law school organizations such as Georgetown's Street Law program. It could also work with professional accounting and legal organizations such as the Tax or Legal Education Sections of the ABA.

The IRS already engages in some educational programs and literature. For example, it has published a series of "fact sheets" on topics that affect many taxpayers such as travel/entertainment expenses, the EITC, Tax Tips (such as for the treatment of a child's investment income) as well as radio public service announcements (in English and Spanish, as well as Country and Western

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92. See Michael Wenzel, A Letter from the Tax Office: Compliance Effects of Informational and Interpersonal Justice, 19 Soc. Just. Res. 345 (2006).



format).<sup>93</sup> Education and outreach programs developed in connection with outside experts could improve the focus and effectiveness of these programs.

### *B. Adopt a “Tax Morale” Model*

The IRS should adopt a regulatory model that incorporates the findings of behavioral compliance research. Unlike the traditional compliance model, focused on enforcement via penalties, this model, acknowledging internal taxpayer motivation for compliance, emphasizes a more individualized carrot and stick approach. It recognizes that different taxpayers have different taxpaying attitudes and behaviors; that these attitudes and behaviors change over time, and that these attitudes and behaviors are affected by interactions with others, including the tax authority. The model seeks to make compliance easier for taxpayers, but strictly enforce penalties when they fail to comply. In devising its model the IRS should not only evaluate the tax morale literature but consult other tax authorities that have instituted such models (such as Australia and New Zealand).

### *C. Establish Educational and Media Programs*

#### *1. Rationale*

Knowledge of mere facts does not necessarily change people’s attitudes nor increase their compliance with norms or laws since people are often guided by heuristics, cognitive processes and other short cuts or rules of thumbs rather than by rational thought. At first glance, then, it might seem that there is little role for education. This is not the case. People can be trained to think logically. Furthermore, the more they know about a subject, the easier it is for them to think and act based on logic and information and not on unexamined biases, frames, and other unconscious cognitive processes. More importantly, information can influence these very processes as well as both social and personal norms.

Education enhances compliance in a variety of ways. Most obviously, people make fewer unintentional mistakes the more they know. They also will be less frustrated when trying to comply with the tax laws. Knowledge gained from education should also decrease a taxpayer’s time spent on taxes which should also decrease frustration and increase compliance. Research shows that

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93. See e.g., IRS Fact Sheet FS-207-10 (Jan. 2007, updated 2/14/07), Deducting Travel, Entertainment and Gift Expenses at [www.irs.gov](http://www.irs.gov) (following “Newsroom” hyperlink; then follow “Fact Sheet” hyperlink); IRS Radio PSAs at [www.irs.gov](http://www.irs.gov) (follow “Newsroom” hyperlink; then follow “207 IRS Radio PSAs” hyperlink); Tax Tips at [www.irs.gov](http://www.irs.gov) (follow “Newsroom” hyperlink; then follow Tax Tips).

education also enhances compliance in more complicated ways that increase tax morale. Various techniques can encourage tax morale in the short term, but as the literature review has shown, many of the attitudes and personal norms that are components of tax morale begin to form early and accumulate over time. Consequently, efforts to improve tax morale must be ongoing and begin in a person's formative years – childhood.

One education program will not suit all taxpayers. People have different learning styles – some learn better visually; others aurally, and so forth. Different audiences also require different content. In some contexts this is obvious; a program for elementary school children must differ from one for adults, for example. A program for native speakers will be different than one for taxpayers whose primary language is not English.<sup>94</sup> A program for tax preparers should be different than one for individual taxpayers. Taxpayers differ on the type of tax information they need, as well as their level of sophistication. There are other differences among audiences, however, that are more subtle, but often not addressed, such as various norms across subcultures. Gender, too, must be taken into account since studies indicate wide differences between genders in risk aversion, moral reasoning, and even responses to compliance appeals. Women, for example, respond more to “friendly persuasion” whereas men respond slightly negatively to this type of appeal.<sup>95</sup>

The IRS must also conduct internal education and training because the literature indicates that taxpayers' perceptions of the tax authority's procedural fairness is an essential component of tax morale. Consequently, training all IRS personnel – especially those dealing directly with the taxpaying public – to be as neutral, objective, polite, respectful, and fair as possible is just as important as training them in the technical aspects of the tax law. Moreover, the adoption of any new procedures, especially those that move from the traditional model with which many IRS personnel are familiar (and so comfortable) to a tax morale model (with which they are less familiar) must be accompanied by intensive personnel training. This training should include not just the specifics of new procedures, but should ensure that personnel understand the reasons for the switch to these procedures and that they commit to them.

Although internal education is vital, the remainder of this section focuses on external education of taxpayers – both current and future ones.

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94. Christine C. Bauman, David Luna & Laura A. Peracchio, *Improving Tax Compliance of Bilingual Taxpayers with Effective Consumer Communication*, 2005 IRS Research Conference 247 (2006)(pictures increased accuracy of bilingual taxpayers).

95. See Chung & Trivedi, *supra* note 73.

## 2. Goals of Education

The goals of educational programs should be both general and specific. They must provide specific knowledge about the role of tax and how the tax system works. Additionally, they should encourage attitudes and behaviors that compliance research indicates are associated with higher tax morale and compliance, such as a sense of civic duty, trust, altruism, integrity.

Providing factual knowledge is fundamental to any educational program because Americans generally are very ignorant about taxation. For example, a 2003 survey by the Kaiser Foundation and Harvard Kennedy School for NPR on taxes revealed that 34% of respondents did not know whether they paid more Social Security/Medicare taxes or income taxes, and only 50% of respondents knew that there had been a tax cut in the past 2 years.<sup>96</sup> Consequently, the IRS, public agencies, schools, and non-profits have a great opportunity to provide information about the tax system generally, including information on changes in legislation, as well as specific information about certain tax provisions. This information could be provided at different levels of complexity to different audiences ranging from elementary school children to tax preparers.

People cannot think rationally about fiscal policy without linking taxation and expenditures. Similarly, they cannot think rationally about taxation without talking about its benefits as well as its burdens. Currently, both politicians and the media emphasize the burdens. Politicians, for example, often claim that the tax burden has increased or is too heavy and, therefore, Congress needs to cut taxes. They rarely mention, however, the benefits of taxation, or the fact that tax burdens are relatively low both historically and relative to other nations. They often talk about taxes generally without differentiating between federal taxes and state/local taxes.

The news media treat taxation in a similar way to the politicians. The media usually fails to differentiate between marginal and effective rates. As another example, NBC Nightly News has a segment called the Fleecing of America that highlights programs that waste taxpayer money; it does not have a segment mentioning programs that benefit the taxpaying public. When a government agency, for example, tracks down the cause of an e coli outbreak, the media does not praise the use of tax dollars, but it will criticize the agency for taking so long to do so – even if the agency's budget has been cut. In short, media and the politicians focus on the negative aspects of taxation for the individual and society, but usually fail to mention the positive good they create.

Although studies show that there is a connection between the perception of public goods and tax compliance,<sup>97</sup> there are grave dangers in linking taxation

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96. Questions 63 and 11 at [http://www.npr.org/news/specials/polls/taxes2003/20030415\\_taxes\\_survey.pdf](http://www.npr.org/news/specials/polls/taxes2003/20030415_taxes_survey.pdf) (33% said there had not been and 17% didn't know).

97. See, e.g., James Alm, Betty R. Jackson & Michael McKee, Fiscal Exchange, Collective Decision Institutions and Tax Compliance, 22 *J. Econ. Behav. & Org.* 285 (1993).

to specific expenditures. First, such a linkage may create a strict benefits or fiscal exchange view of tax. A narrow fiscal exchange view may lead some taxpayers to perceive exchange inequality which, in turn, may cause them to see taxation as unfair. Once they see the tax itself as unfair, they may be less willing to pay. Second, people frequently do not agree on whether a particular expenditure is worthwhile. Consequently, linking a certain amount of tax to a certain good or service may decrease a taxpayer's willingness to pay the tax if s/he does not value that particular program.

There are ways to minimize this danger. General discussions about the concept of "public goods" might, for example, make citizens more amenable to taxation. Other possible solutions are listed below. Some of them relate specifically to tax; others encompass the role of government, generally. Most of them require sustained educational campaigns because components of tax morale, such as trust, take a long time to build – even though they may deteriorate quickly. Since many tax morale components involve schemas and affective qualities that develop early in life; some educational programs should be directed at youth – long before they become taxpayers. Various school curricula in social studies or economics, for example, are ideal places for children to learn about the role of taxes in society and to become tax literate.

People acknowledge that voting and jury service are civic responsibilities (although often honored in the breach), but rarely think of taxation as one. Education campaigns could help change this view. Once paying tax is viewed in this light, people could be encouraged to take pride in doing so, just as they take pride in voting or helping their place of employment reach United Way goals. For example, taking a cue from get-out-the vote-campaigns, they could also have stickers saying "I paid my taxes today."

The literature indicates that certain characteristics correlate with higher tax compliance, such as trust, reciprocity, a sense of national identity and altruism. The IRS could incorporate aspects of this research into its educational campaigns.

Research indicates that high moral reasoning correlates with higher tax compliance and that education is an important factor in increasing moral reasoning. These connections suggest that education in ethics and moral reasoning could improve compliance. At least one study suggests this: "[E]ducation . . . may improve tax compliance. Further, the results also highlight the importance of encouraging and maintaining a positive attitude towards governments amongst the general population to achieve a tax compliant population. Thus, policies that encourage/emphasize education and ethical behavior may be an effective method of increasing the level of taxpayers' compliance."<sup>98</sup>

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98. Trivedi, Shehata & Lynn, *supra* note 22, at 193.

### 3. *Examples of Specific Educational Programs*

#### *a. Design Curriculum for Schools*

States and school districts prescribe curricular guidance for grades K-12 in various subjects including civics, social studies, and economics. Although taxes are integral to all these topics, taxation usually plays little or no role in the curriculum. The IRS, in conjunction with educational and curricular experts, could devise curriculum appropriate for all ages. There are various less traditional ways to present this information. For example, many law schools have a Street Law Program in which law students teach high school students about various aspects of the law. Media popular with the young – such as videos and the internet – could also be used. In 1998, for example, the Federal Reserve Bank of New York published a comic book describing how foreign trade works.<sup>99</sup>

#### *b. “Deliberation Day” Discussions*

In their book *Deliberation Day*, Bruce Ackerman and James S. Fishkin propose town hall type meetings before presidential elections to discuss the candidates and issues. Similar type of meetings could occur at the start of tax season, in town hall meetings, and/or on television, radio and the Internet.

#### *c. An Annual Income Statement*

Every year the Social Security Administration provides a short explanation of how social security works and a summary of a taxpayer’s past contributions and potential benefits. A similar pamphlet distributed annually by the IRS might help taxpayers both understand the system better and feel more ownership.<sup>100</sup>

### 4. *Specific Recommendations regarding Media Campaigns*

The IRS should conduct an extensive media campaign regarding taxes in order to reach the widest number of the public. Some of these campaigns should focus generally on taxes while others could concentrate on specific tax issues. The EITC outreach program is a good start for a model, but the suggested campaign must go beyond that in terms of media outlets, content, and purpose. The campaign’s goal should be to encourage values and norms that enhance tax compliance not simply to convey tax information. The campaign

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99. Cedric Fan. *The Story of Foreign Trade and Exchange* (1998).

100. Marjorie E. Kornhauser, *Doing the Full Monty: Will Publicizing of Tax Information Increase Compliance?*, 18 *Can. J. L. & Juris.* 95 (2005).

should seek to develop those values and norms, discussed in the literature review, that are connected with high compliance including trust in the government and a sense of civic duty to pay taxes. It should also stress the competency of the IRS. Many taxpayers may not question the honesty of IRS officials, but they may doubt the efficiency and/or ability of IRS personnel.

The danger of a media campaign, like the danger of an education campaign, is that it could backfire. It might cause taxpayers to feel manipulated, which would increase cynicism and potentially more non-compliance. In order to prevent (or minimize) these negative consequences the IRS must move cautiously and with the aid of outside experts.<sup>101</sup>

Successful marketing engages many of the same principles that enhance tax morale, such as reciprocity, norms, and trust in authority.<sup>102</sup> Marketing campaigns also use many tactics that would be helpful in campaigns to improve tax compliance, such as formulating suggestions in the positive not negative. The following suggestions indicate some of the possibilities of a marketing campaign.

*a. Public Service Ads Using Marketing Principles*

Public Service campaigns should target specific market so that different types of taxpayers receive different ads. Ads would vary in both form and content. Content could be varied to target the characteristics of different demographic taxpayers, as shown in the research. The form should also match the target audience in language and media use. Appropriate language is not just limited to whether the campaign should be in English or another language, such as Spanish. Even within a group that speaks the same language, word style and slogans appropriate for one sub-population – such as the elderly – will not be the most effective usage for a group in their early 20s, for example. Similarly, the most effective media for one group (e.g. newspapers) will not be the most effective media for the internet-savvy younger generation.

Ads should harness the power of particular people to influence others. Politicians, advertisers and even charities know that a celebrity spokesman can influence others to support their project (or buy their product). The IRS should use similarly influential people to support paying taxes.<sup>103</sup>

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101. See, e.g., Tax Report to the Treasurer and Minister of Revenue by a Committee of Experts on Tax Compliance (1998) Chapter 16 Relationship with Taxpayers, ¶¶ 16.33-16.36 at [www.taxpolicy.ird.govt.nz/publications/files/html/coe/chapter16.htm](http://www.taxpolicy.ird.govt.nz/publications/files/html/coe/chapter16.htm).

102. See, e.g., Cialdini, *supra* note 8, at 205-220 and Cialdini, *supra* note 56.

103. See, e.g., Malcolm Gladwell, *The Tipping Point: How Little Things Can Make a Big Difference* (2000) (discussing what he calls the “law of the few” in which the messenger is as important as the message.)

*b. Use the Internet and Videos*

Tax campaigns should employ the Internet's well-known ability to reach large numbers of people. For example, in 2007 Turbo Tax made unique use of the internet and fascination with YouTube during the 2006 filing season by sponsoring a rap video contest, with an award of \$25,000 for the best tax video. (Interestingly, no mention is made on the webpage that the prize is taxable.) The contest was introduced in a rap video called Turbo Tax Mojo by Vanilla Ice,<sup>104</sup> urging people to pay their taxes (on time!) and of course use Turbo Tax to do so. Less than one week after the contest started (8 February) 37 videos were posted.

*c. Creative Use of the Media and Media Talent*

In World War II, the government used Donald Duck to persuade Americans to pay their income taxes. The IRS could similarly encourage the development of tax themes in TV shows or other mass media, either as a small segment or even the theme of an episode, as occurred a few years ago on the Simpsons. People acquire a great deal of information from entertainment on television, not just from news programs. They also act upon it. For example, after viewing episodes about breast cancer on ER, one study showed that viewers were more likely to schedule a breast screening exam than non-viewers.<sup>105</sup> In 1989 Robert Cialdini suggested a TV special, which he labeled, the National Tax Test, airing one month before April 15th after the earlier television show, the Great American Values Test.<sup>106</sup> Today, with the reality and game shows so popular, his idea could be expanded into a series of episodes modeled either as a reality show or a game show.

*D. Additional Specific Recommendations*

There are many promising areas of research – some basic research and others more narrow implementation of theoretical findings. The following focus on the more practical aspects and are in no way meant to be comprehensive.

*1. Demographic Factors*

The IRS and theoretical research have already begun identifying various segments of the taxpaying population that have different characteristics.

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104. Available at [http://www.youtube.com/watch?v=Y2hZS\\_ZRZHY](http://www.youtube.com/watch?v=Y2hZS_ZRZHY). (viewed 13 February 2007). For the rules see [www.youtube.com/contest/thetaxrap](http://www.youtube.com/contest/thetaxrap).

105. See, e.g. Stephen Smith, The doctor is on. Boston Globe, 12 Dec. 2006 at C1.

106. Cialdini, *supra* note 8, at 209.

The BSU should continue this work and then devise strategies that build on this new knowledge.

### 2. *IRS Procedures to Improve Procedural Justice*

The literature contains many studies concerning the importance of procedural justice in tax morale. Some experimental research has already been conducted in the field of communications with taxpayers, such as the effect of various form letters on compliance. The BSU should continue to explore and experiment with various procedures and strategies that would improve taxpayers' sense of fairness. These range from improving IRS contact with taxpayers (whether by letter, in-person or phone contact) to training personnel to treat taxpayers with more respect and politeness – factors that influence tax morale. The following suggestions are illustrative of a few of the many issues the BSU might investigate.

### 3. *Reconsider Nomenclature: Customer v. Taxpayer*

The literature on behavioral compliance suggests that the IRS should reevaluate the term it uses for a person who pays taxes. In recent years, many collection agencies, such as the IRS have emphasized the term “customer” instead of “taxpayer.” The two terms may provide different signals and therefore influence taxpayers and IRS officials differently.

The term *taxpayer* may have both positive and negative effects on IRS personnel.<sup>107</sup> On one hand, using the term *customer* may improve how personnel treat taxpayers because it lessens any bureaucratic or authoritarian impulses. On the other hand, calling taxpayers customers has negative effects. First, given the often poor state of customer service, IRS officials may simply treat taxpaying *customers* with the same poor service they may have received as customers in stores. Furthermore, “customer” transforms a taxpayer into an isolated purchaser and not a citizen performing a civic obligation. This devalues the civic duty aspects of paying taxes and the greater identification with the nation as a whole which, research has shown, makes a taxpayer more likely to comply.

By turning paying taxes into a commodity like buying pizza, the term *customer* may decrease tax morale by “crowding out” internally motivated compliance behavior that derives from intrinsic personal norms, such as integrity and patriotism. If the taxpayer is merely a customer, then paying taxes is no different than paying off a car loan, except that the IRS may be viewed more hostilely than other creditors because it carries a bigger stick. Moreover, if a tax debt is no different from a car debt, the individual will see these greater

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107. See, e.g., New Zealand's Tax Report to the Treasurer and Minister of Revenue by a Committee of Experts on Tax Compliance, *supra* note 101.



enforcement powers as unfair or even evil and violating the individual's constitutional rights and therefore un-American.

The term *taxpayer*, on the other hand, emphasizes the civic responsibility of taxpaying and confers dignity and respect on the taxpayer. Being treated in this manner can heighten a taxpayer's sense of fairness, according to research, and therefore increase tax morale and tax compliance. A taxpayer is different from a customer buying a pizza. The term taxpayer distinguishes the two transactions and adds both seriousness and a dignity to the individual and the transaction.

#### 4. *Compensatory Measures, Including Apologies*

Taxpayers can develop especially negative feelings about the IRS and taxes when there is a dispute about the proper amount of tax owed, or even if there is just an unpleasant interaction with IRS personnel. Marketing studies of complaint procedures provide insight regarding efforts that help reduce negative attitudes towards firms and improve customer loyalty. Although the IRS, being a monopoly with which all taxpayers must deal, need not worry about its customers abandoning it for a competitor, the IRS must still worry about taxpayer satisfaction. Discontented taxpayers may minimize what they owe, pay their bills only after lengthy (and expensive) IRS procedures, and some taxpayers may fail to pay any taxes at all. Dissatisfaction with IRS procedures, in short, decreases tax morale which adversely affects compliance.

The IRS can apply knowledge and techniques that firms have developed to increase to customer satisfaction and brand loyalty when confronted with complaints. Positive procedures identified through research and experience include (1) compensation measures (e.g. refunds, replacements, repairs), (2) responsive employee behavior (especially "empathy, politeness, and an effort to listen"), and (3) prompt responses.<sup>108</sup> The last two factors are easily applicable in the tax context, but even the first – compensation measures – may be applicable in the tax situation, especially if compensation is broadly construed to include emotional compensation such as apologies, or extra help, or faster service next time.

Apologies can range from simply acknowledging a taxpayer's inconvenience or regretting the inconvenience to an admission of negligence or even wrongdoing. Both the IRS and the taxpayer will react differently to different types of apologies. This is an area worth investigating.

#### 5. *Shaming/Publicity*

Some states now publicize the names of delinquent taxpayers as a "shaming" device. Although the literature indicates that shaming may have

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108. Estalami, *supra* note 46, at 289.

mixed results, the BSU should both investigate the results states have produced and research the implications and effectiveness of shaming more generally.

### *6. Rewards*

Although economic incentives can backfire and decrease compliance by “crowding out” internally motivated behavior, rewards – broadly construed – may still have a role to play, if carefully constructed. Monetary rewards, such as rebates of a percentage of the tax, can be counterproductive. They may decrease (crowd out) internal motivations to comply because the taxpayer may consider them discounts, like rebates in a commercial setting, and thus ones to which s/he is entitled. On the other hand, a taxpayer may view a non-monetary reward which is not based on the amount of tax paid more favorably and see it simply as an acknowledgment of good behavior. This type of reward, research suggests, may not decrease morale. Some compliance experts have suggested various types of these rewards that would indicate appreciation of good citizenship without commoditizing taxpaying and decreasing tax moral, such as reduced public transportation fares, or free admission to museums and cultural events.<sup>109</sup>

There are other possible rewards of this nature. Taxpayers who have paid the correct amount of taxes in a timely fashion for a stated amount of time, for example, might be given faster access to assistance such as special phone lines that have a shorter wait. This approach is less drastic, and perhaps more acceptable, than Professor Joshua Rosenberg, University of San Francisco School of Law, recent suggestion of rewarding taxpayers who provide extended reporting, with lower tax rates.<sup>110</sup>

It is possible to integrate rewards with sticks. HMRC, for example, is toying with the idea of requiring individuals to show a certificate of tax compliance to renew certain licenses like taxi licenses.<sup>111</sup> Certainly, all federal employees and independent contractors could be required to show that they are current with all taxes, and perhaps, have not been delinquent for a specified amount of time.

### *7. Tax Preparer Education and/or Registration Requirements*

Many professions require continuing legal education. California is now requiring preparers to register with the California Tax Education Council, which

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109. Feld & Frey *supra* note 42, at 111.

110. Tax Gap Stakeholders Debate Tax Gap Elements, Differ on Methods to Improve Compliance, BNA Daily Tax Report, June 25, 2007 at G-8.

111. Interview with Simon Norris, head of Review of HMRC Powers Team in HMRC Business unit (Central Policy) and Gordon Smith, Deputy Director of Debt Management & Banking, and Georgina Halligan, Process & Strategy of Debt Management & Banking, May 23, 2007.

requires continuing education and maintains a code of conduct.<sup>112</sup> Although many preparers – such as accountants – are members of a profession that already requires CLE, that education may not address tax compliance issues specifically or in a manner that focuses appropriately on the topic. CLE specifically targeting preparers might better improve compliance. CLE has many critics, including those who claim it is ineffective; people attend, for example, but read the newspaper instead of listening. Certain types of CLE address these deficiencies more than others. For example, those requiring the practitioner to pass a test should improve knowledge better than those that merely require attendance.

## V. CONCLUSION

Behavioral research about compliance generally and tax compliance specifically holds much promise for improving voluntary tax compliance. Since it is a rapidly growing and complex field, the IRS can best take advantage of its findings by dedicating – on an ongoing basis – time, money and personnel to it. This Report contains three major recommendations: 1) the IRS establish a Behavioral Research Unit which would keep abreast of current developments, conduct independent research, supervise contract research, and help implement findings throughout the IRS; 2) the IRS adopt a tax morale model of tax compliance that recognizes that taxpayers have varying attitudes and behaviors regarding tax, and match IRS behavior with that of taxpayers; and 3) the IRS engage in educational efforts aimed at all segments of the population to improve taxpayer knowledge, attitudes, and behaviors. The Report also suggests, as examples, several areas that merit further exploration.

Applying the findings of behavioral research is essential to maintaining and improving compliance, but it also carries a grave danger: the possibility that the public – or portions of it – will interpret the use as manipulation. In the commercial setting, people are cynical about manipulation through behavioral research, but accept it as part of the marketplace. They are less accepting in the public sphere and cynicism here can backfire and cause a decrease in compliance. In order to forestall such cynicism, the IRS must both act and be seen as acting sincerely. Research indicates that strict adherence to procedural justice and to respectful modes of communication will help. The BSU, however, must continue to research this aspect, too.

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112. Speakers Support Multifaceted Approach, Incremental Steps to Combat the Tax Gap, BNA Daily Tax Report, June 25, 2007 at G-10.